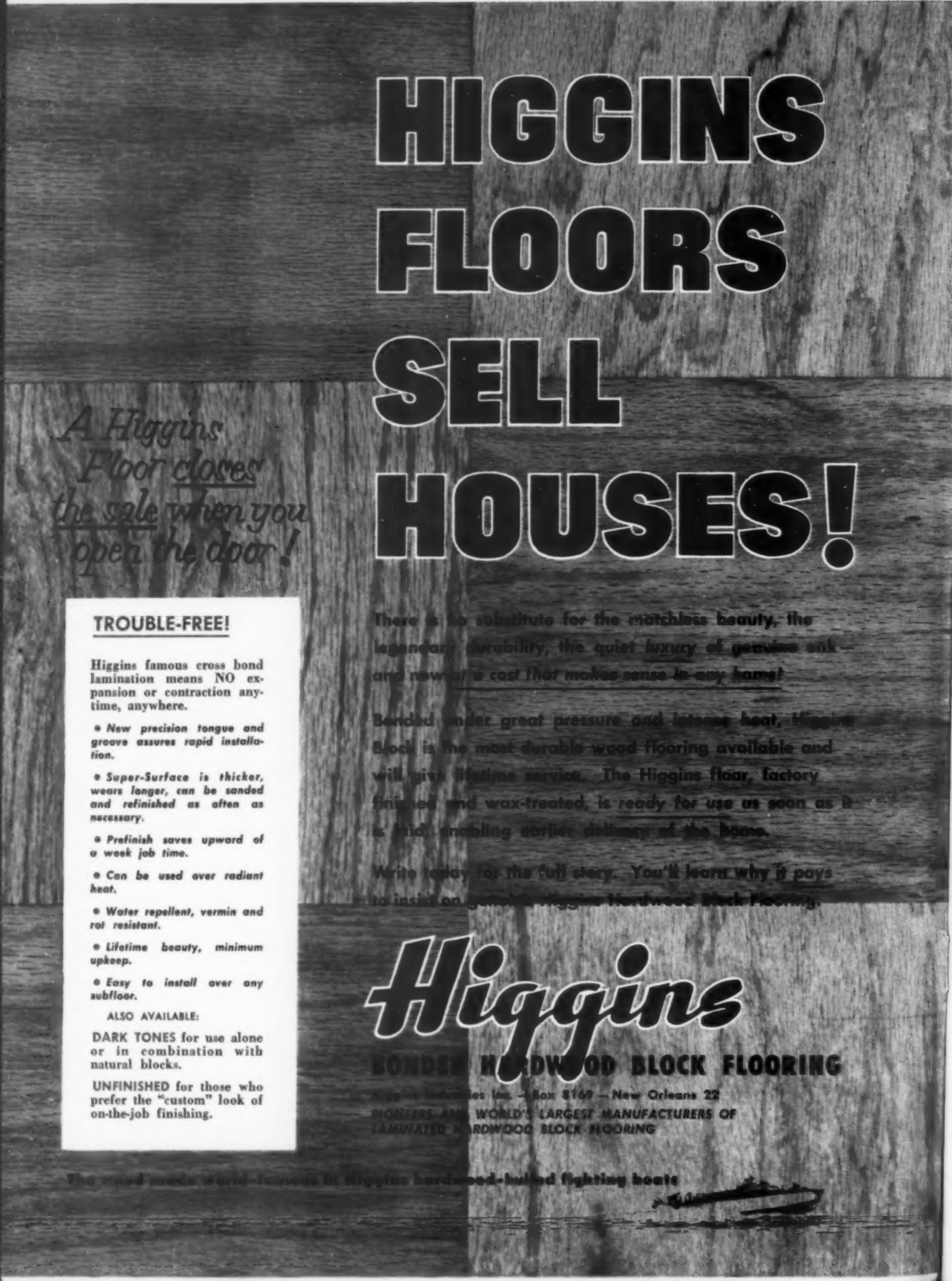
The Mortgage Banker

in this issue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The Dairy Country

MBA 1957 Calendar

February 19-21, Midwestern Mortgage Conference and Farm Mortgage Clinic, Conrad Hilton Hotel, Chicago

February 22, Board of Governors Meeting, Conrad Hilton Hotel, Chicago

March 14-15, Mortgage Servicing Clinic, Statler Hotel, St. Louis

March 21-22, Southern Mortgage Conterence, Hotel Roosevelt, New Orleans

April 15-16, Eastern Mortgage Conference, Commodore Hotel, New York.

April 25-27, Southwestern Mortgage Clinic, Paradise and Jokake Inns, Phoenix

April 30-May 1, Mortgage Servicing Clinic, Biltmore Hotel, Los Angeles

May 15, Board of Governors Meeting, Golden Gate Hotel, Miami Beach.

May 16-18, Southeastern Mortgage Clinic, Golden Gate Hotel, Miami Beach

June 23-29, School of Mortgage Banking, Courses I and II, Northwestern University, Chicago

June 30-July 6, School of Mortgage Banking, Course III, Northwestern University, Chicago

July 28-August 3, School of Mortgage Banking, Course I, Stanford University, Stanford, California

August 4-10, School of Mortgage Banking, Course II, Stanford University, Stanford, California

November 4-7, 44th Annual Convention, Statler Hilton Hotel, Dallas

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THIS MONTH'S COVER

The Mortgage Banker looks in on the annual dinner meeting of the Chicago MBA, one of the oldest and largest of the nearly 50 local mortgage groups of the country. For a report of what was said, business transacted and a bit of historical background of the Chicago Association, along with a recap of the status of local mortgage groups over the country, see pages 45-46.

The Mortgage Banker

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Volume 17 **FEBRUARY, 1957** **Number 5**

Contents

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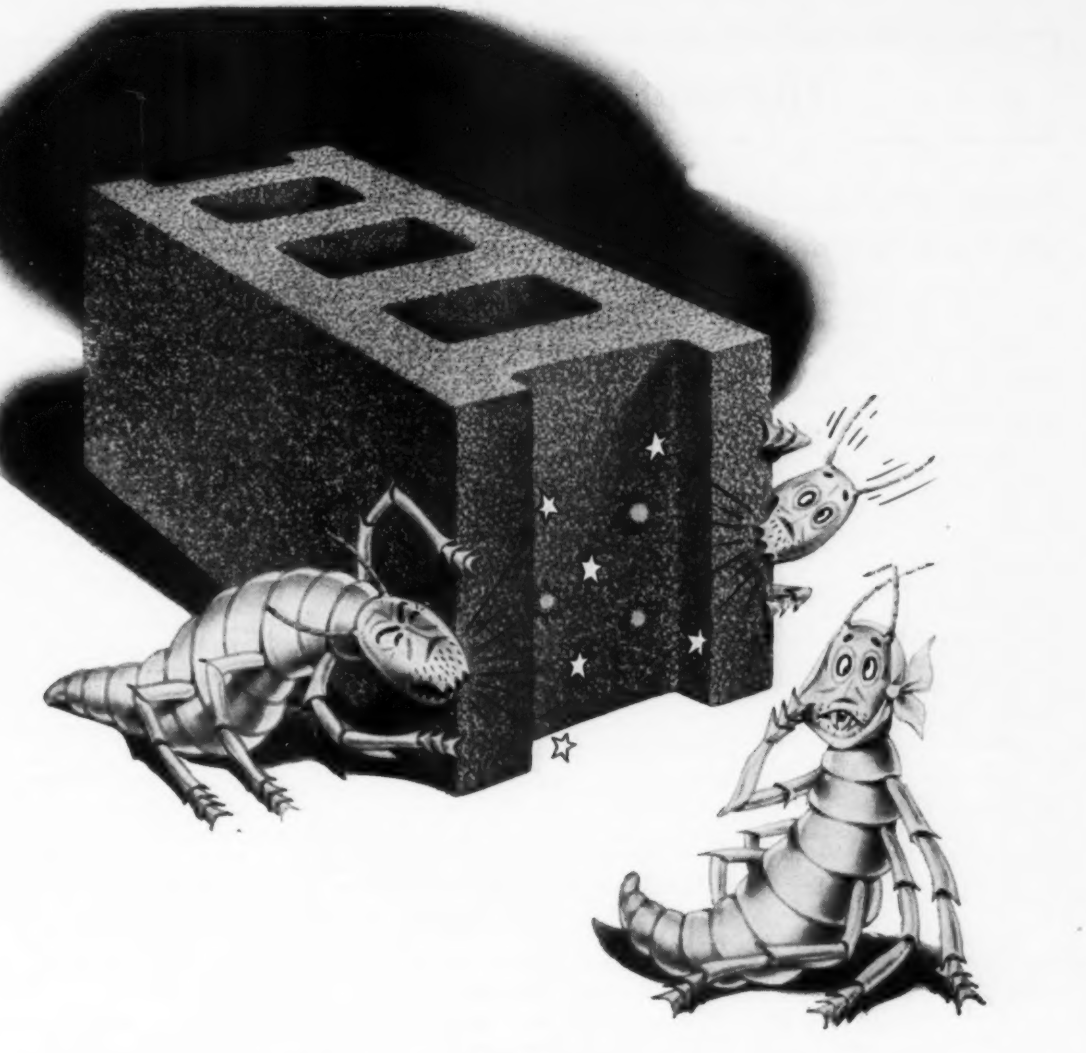

THE *tormented* TERMITE

This is a drawing of termites trying to gnaw a concrete block and making absolutely no progress.

No matter how many termites attack a concrete masonry house, or how long they work at it, the concrete will be unimpaired, as solid as ever. That's why a concrete masonry house is a good place for mortgage dollars.

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Wider Markets, Improved Products and More Of Total Building Characterize the Prefab

Through its steady, consistent improvement, prefabricated housing is becoming an increasingly greater challenge to all builders, with the entire home buying public the leading beneficiary of the competition, the annual prefab survey issue of House & Home observes.

The survey shows that more than 75 per cent of prefab manufacturers now retain registered architects to design their houses. This design improvement trend "means not only that prefabs will be better to live in and better to look at—it also means that those who compete with prefabs will be forced to turn out a better product."

Citing the improved production techniques being developed throughout the prefab industry, it is pointed out how these also exert an important influence for the better on all home building.

"For what the prefabbers are doing to industrialize home building, is duplicated by on-site builders throughout the country. Or, if it isn't, it had better be soon! For unless U. S. home builders start producing more with less labor and less waste of materials, the industry will not cash in on more than a small part of its vastly expanding potential market.

"Prefabrication's 7 per cent of the home building market may be a drop in the bucket, but that drop begins to look like a pretty powerful dose of good medicine. It's a dose that has done much to change home building to date, and will do a lot more to change home building tomorrow."

Marketwise, prefabbers ended 1956 with the production of about 70,000 units, compared with about 93,000 in 1955. For 1957, however, industry leaders look for a production upturn again to 100,000 to 115,000 units.

Pointing out that more than 80 per cent of prefab houses were usually sold with FHA and VA financing help, it is noted that prefabbers fared relatively better than other builders working in the FHA and VA sector of the market in 1956 "although prefabbers' output was down 23 per cent for 1956, total VA starts fell 32 per cent and FHA starts tumbled 44 per cent. Perhaps one of the reasons prefabbers were better able to deal with red tape of the government mortgage market was the part played by the larger firms and the services they were able to give their builder-dealers."

An unexpected source of increased prefab sales last year was in the bigger, higher-priced house market. "Producers climbed the price scale and tapped a second-time buyers' market that once belonged only to the custom-house builder. The best selling models were often the bigger houses. Prefabbers are preparing to build more of them this year and also offer new low-price models in an effort to revive the low-cost market."

Survey data for 1956 showed that prefab sales are moving East faster than West, with five of the top ten states in prefab sales now in the East.

Ohio, Illinois and Indiana, where prefabrication got its first real roots, still continue to take almost half of total production, but now New York ranks 4th in the nation, with Pennsylvania, New Jersey and Maryland standing 6th, 7th and 8th respectively. Michigan, Missouri and Virginia are 5th, 9th and 10th in sales.

Prefabrication sales are also developing strength in Iowa, Louisiana, Minnesota and Wisconsin. Georgia and Florida still hold a share of the market, and Massachusetts, Connecti-

cut, North Carolina and Alabama are gathering momentum.

"Prefab's speed, its control over costs and its financing helps are primarily responsible for opening up the Eastern market. Rising costs in the East have reduced the edge that highly competitive builders and subcontractors used to have over prefabricators. The wide variety of designs available in prefabs has also helped to break the East's resistance.

"While the same factors apply to other areas of the country where prefab sales are building up, the East is important because of its population concentration.

"Prefab plant locations closely correlate with sales areas because overnight trucking radius still is the best maximum distance for prefabbers to ship. If a truck loads by day, travels at night, and can unload first thing in the morning, both prefabber and dealer save money. Trucks are kept moving, plant labor kept busy and construction crews at the site are not waiting around at $2.50 to $3.50 an hour."

Third Life Company Funds in Mortgages

Last year, 31.8 per cent of life insurance assets were in non-farm mortgages as against 30.1 per cent in 1955, 28.3 per cent the year before that and 27.3 in 1953. Farm mortgage holdings for the last four years were 2.6, 2.5, 2.4 and 2.4 per cent. Government securities dropped from 12.5 per cent in 1953 to 7.9 per cent at the end of last year.

What is the outlook for life company investments for this year and beyond? Dr. James J. O'Leary, director of the Life Insurance Associa-

tion of America, in his report to members, analyzed it as follows:

"During the past two years the exuberance of our national economy has led to enormous demands for capital funds which have overflowed the supply of savings. The inevitable outcome has been to create strong pressures for an increase in commercial bank credit beyond the requirements of normal growth in our national economy. In the field of residential and industrial construction, state and local improvements, and consumer durable goods we have been pressing to expand beyond our resources. Here is the fundamental source of upward pressure on prices, and under the circumstances it has been salutary for the monetary authorities to restrain the expansion of bank credit."

Looking forward to 1957, Mr. O'Leary declared "there is little reason to expect this situation will alter appreciably. It now seems clear that we shall again be confronted with demands for capital funds in excess of available supplies from nonbank sources, and that the monetary authorities will be required to continue a policy of credit restraint. Although we may well continue to experience the 'rolling adjustments' in general economic activity which have characterized recent years, all signs now indicate that over-all business activity will remain high this year and that gross national product will increase moderately to a new record level. Consumer expenditures, bolstered by a comeback in the automobile market, as well as business expenditures, should continue strong. In the face of increased international tensions, Federal expenditures may well be pushed upward.

Long Range Planning

"Although the current rate of plant and equipment expenditures by business concerns is very high, there is little evidence from surveys carried out by McGraw-Hill, the Department of Commerce, and others that we can expect any marked abatement in 1957. More and more attention is now being directed by economists to the longer-range view being taken by business executives in planning expansion and improvement of plant and equipment, as well as the great impact of industrial research on business capital spending. Rising borrowing costs of corporations can easily be exaggerated because interest rates are still low historically and in relation to profit expectations. Moreover, despite all the talk about a decline in residential construction this year, there are good prospects that housing starts will run as high as one million or slightly higher, so that it still appears that total uses of mortgage funds—residential, farm, and industrial-commercial—will be as high as in 1956.

"The demand for capital funds by state and local government units promises to remain high, particularly in view of projects which had to be postponed in 1955. If we do experience a resurgence in the automobile market an upward push will be given to the demand for consumer credit. Underlying the entire capital market picture is the fact that at the end of last year there was a sizable overhang of capital expenditure projects which had to be postponed because of

a scarcity of available funds at desired rates. Added to this, the great pressures of demand for funds have gradually reduced liquidity in the financial system as a whole, including both the commercial banks and nonbanking institutions."

In view of this outlook, Dr. O'Leary said "it is difficult to avoid the conclusion that 1957 will again be a year in which the various demands for capital funds will overflow the supply from nonbank sources, and there will be great pressure for an expansion of bank credit beyond growth requirements to fill the gap. Market forces, therefore, should produce firm to rising interest rates. We should witness the continuation of a policy of credit restraint by the monetary authorities designed to head off an inflationary increase in commercial bank credit.

"The Federal Reserve and the U. S. Treasury have wisely and courageously pursued a policy of credit restraint to keep our national economy on an even keel and to maintain stability in the value of the dollar. There is nothing in the outlook for 1957 which would reduce the great public need for a nonpartisan, fully independent Federal Reserve — free to study economic trends and to determine monetary and credit policy responsibly and objectively in the broad public interest. The country is fortunate that we have had such freedom on the part of the monetary authorities, and they have pursued wise policies. But we must always remember that the Federal Reserve and the Treasury sorely need the aid of other public and private groups if we are to have stable and sustainable economic growth. Restraint by the monetary authorities must be matched by restraint on the part of business concerns, organized labor, the consumer, lending institutions—indeed the country as a whole."

In his report to the members he explained the changing composition of the life insurance investment portfolio for the period 1953-1956. Among the many changes revealed is the drop in government securities holdings and the increase in stocks and nonfarm mortgage holdings.

Current Status in Rents and Building

» **RENTAL STATUS:** Demand is mounting for the better rental units accompanied by increasing vacancies in deficient dwellings, NAREB's new survey shows.

The study made in 234 communities disclosed:

» Residential rents have stabilized in the majority of communities, but where change occurred in 1956, the prevailing movement for most types of units has been upward.

» Overall vacancy rates did not change appreciably during 1956.

» The offering of rental concessions has not become prevalent in many communities, although redecoration and routine maintenance are now a part of normal practice in more places.

Representative comments disclosed vacancies to predominate in such categories as poorly maintained buildings, basement apartments, garage apartments, wartime conversions, older type units where modern facilities are lacking, units in undesirable locations, and minimum type apartments built during the war.

For moderate-priced elevator buildings, rents are reported to be the same, compared to a year ago, in 72 per cent of the areas, higher in 23 per cent, and lower in 5 per cent.

For apartments in de luxe structures, rent levels are similar to those prevalent a year ago in 65 per cent of the communities and higher in 30 per cent.

For units in garden-type developments, charges are about the same as a year ago in 72 per cent of the areas and higher in 25 per cent.

For walk-up apartments, rents remain constant, compared with a year ago, in 64 per cent of the communities, but are lower in 21 per cent and higher in 15 per cent.

For converted units in older dwellings, the rent picture is the same as a year earlier, according to 44 per cent of the reporters, but shows a smaller price tag in 42 per cent of the areas and a higher one in 14 per cent.

Tenants of single-family structures are paying about the same rents as a year ago in 62 per cent of the communities, but the trend has been upward in 30 per cent and downward in 8 per cent.

Vacancy rates on the whole did not change much during 1956. In most cities new construction has added volume and quality to the housing supply, and the units have been readily absorbed into the inventory. An increasing number of junkers has been demolished, and the sites cleared for nonresidential use or for residential reuse. Other obsolete or dilapidated structures are standing vacant.

Occupancy levels of habitable rental units have continued to be high in most cities, with 59 per cent of the communities listing vacancy rates of 2 per cent or less, and 28 per cent of the areas reporting rates of 3 to 5 per cent.

» **RECORD BUILDING:** Last year set a new record in dollar volume of contract awards for future construction in the 37 states east of the Rockies, F. W. Dodge reported. At $24,412,630,000, the awards were 3 per cent greater than the 1955 total.

However, December awards at $1,575,897,000 were 18 per cent lower than December 1955 and marked the fourth consecutive month in which awards were lower than the corresponding periods of 1955.

The cumulative awards for 1956 also established all-time records in dollar volume in two major construction categories: non-residential awards at $9,005,948,000, were 6 per cent greater than the similar 1955 period; heavy engineering at $5,580,-222,000 showed a 10 per cent increase. However, residential awards at $9,826,460,000 were down 4 per cent compared to 1955 although they were the second highest ever recorded.

Thomas S. Holden, Dodge vice chairman, said: "While contract awards in the past year set records, the increase was more moderate than

in any earlier postwar year. This is not at all surprising, and in fact it was anticipated in our outlook statement issued in November 1955. The prospects for 1957, at this stage, seem to be for another moderate increase to new record levels, sparked largely by public works construction of all types, with particular emphasis on highways."

December awards by major construction categories show a new record in dollar volume in the heavy engineering category of $502,029,000, up 4 per cent compared to December 1955. However, residential awards at $450,646,000 were down 37 per cent, and non-residential at $623,222,000 decreased 14 per cent compared to the like 1955 period.

Flexibility Rates In Canadian Loans

Back in December, in this space, we observed that Canada had demonstrated how flexible interest rates work by tying its bank rate (same as our discount rate) to the yield set each week by the turnover in Canadian treasury bills. Actually there is in Canada an even more striking example of how flexibility works than we knew at the time—and are indebted to S. A. Shepherd, manager of the mortgage department of the Bank of Montreal in Montreal, for telling us about it.

"We have what might be termed a semi-flexible interest rate in government-insured mortgage loans under our National Housing Act, 1954," he said. "These loans (similar in principle and in many details to your FHA's) are made at a rate of interest which is subject to a maximum established by the Government by Order-in-Council in accordance with Section 4 of the Act, which states that 'The Governor-in-Council may by regulation prescribe the maximum rate of interest payable by a borrower in respect of a loan to be made under the Act'. It goes on to say that 'The rate of interest prescribed . . . shall not exceed the interest rate on long-term Government bonds . . . by more than 2¼ per cent.' The 'interest rate on long-term Government bonds' is defined as the rate of interest return that would be yielded in the market by Government of Canada bonds that, at the time the maximum rate of interest is prescribed, would mature in 20 years, taking the most comparable issues of Government of Canada bonds in the market.

"The effect of this arrangement is that the Government, at time of fixing the maximum, must not exceed the 2¼ per cent margin referred to, and that the Government may change the maximum rate at any time the stated margin permits it. However, action to change the rate is not compulsory.

"Since the maximum rate was established in March, 1954, we have had two changes in it—down to 5¼ per cent on February 17, 1955, and back to 5½ per cent on March 12, 1956. While the maximum was at 5¼ per cent some lenders were making loans at 5 per cent. Once set, of course, the interest rate stays the same for the life of the particular loan."

Birth of New Idea In Shopping Center

Working rather quietly but nevertheless furnishing leadership in the field, an MBA member, James W. Rouse of Baltimore, has become one of the top authorities in shopping centers. His has been no small-scale effort—he has developed some of the

largest and most successful centers in the country and the innovations in design and concept he has sponsored have been numerous.

Now he has come up with something else that is new—his firm, James W. Rouse & Co., Inc., in company with three builders in his city, Jack Meyerhoff, Harry Bart and Albert Stark, have formed a new company to engage in the development of shopping centers.

The company, Community Research and Development, Inc., will build, own and operate shopping centers at various locations throughout the country.

The four initial projects will be the construction of shopping centers in Easton, Glen Burnie, and Baltimore, Md., and in Charlotte, N. C. Also new is the financing which has been done publicly—only the second case of this kind we have observed.

A new issue of $3,000,000 of 6 per cent convertible debenture bonds, issued by the company, has been offered to the public.

Rouse has financed 33 shopping centers having over 3,000,000 square feet of gross area, and also has served as consultant for many shopping centers.

Jack Meyerhoff has been in the building business for more than 30 years.

Both Mr. Bart and Mr. Stark have also been engaged in the building business for over 30 years. Mr. Bart was one of the two contractors for the Mondawmin center in Baltimore and is one of its principal owners.

Directors of the new company include Samuel E. Neel, of Washington, D. C.

An unusual feature of the financing is that the debenture bonds will be convertible, at the option of the buyer, into either one of two packages of preferred and common stock.

After January 1, 1959, each $1,000 bond may be converted by the holder into either preferred stock with a redemption value of $2,000 plus 90 shares of common stock, or into preferred stock with a redemption value of $1,000 plus 210 shares of common stock. The bonds will mature in 15 years.

What Nehemiah Said to the Mortgage Men

A Thought from the Distant Past Applicable for Today

THERE is only one place in the Bible where the word mortgage is found. It is in the book of Nehemiah in the Old Testament. This book should be interesting reading for the mortgage investors and mortgage bankers of the present day.

After the captivity in Babylon the Jews began to go back to Jerusalem. This name is from two Hebrew words Yeru and Sholem, which mean City of Peace. There must be some sort of Jewish humor in this name because there has been fighting in Jersualem almost continuously for the past 3,000 years and it is still going on there.

The head man at Jerusalem during this period was named Nehemiah. This is also two Hebrew words, Nehem and Yah, meaning Friend of Jehovah. People had religious names then even as they have today.

When the Jews rebuilt their houses they needed money and borrowed it, giving mortgages as security. But Nehemiah wanted them to also rebuild the walls and gates of the City to keep out the warring tribes who lived in the neighborhood. Nehemiah's story in his own words:

"I went out by night and viewed the walls which were broken down and the gates thereof. And I said ye see how the gates were burned with fire. Let us build them up."

So Nehemiah went to the home

owners and asked them to give him money and men to rebuild the walls and provide new gates. But the home owners said they were not interested. As a matter of fact they were not the owners of the houses at all because their homes were mortgaged up to the hilt and actually the mortgagees owned the houses. Furthermore the mortgages were not only on their houses but even on their children. It seems that mortgagees wanted plenty of security in those days. Says Nehemiah:

"And there was a great cry of the people, who said, we have mortgaged our lands, vineyards and houses that we might buy grain, we have borrowed money for the king's taxes and that upon our lands and vineyards. We brought into bondage our sons and daughters neither is it in our power to redeem them, for other men have our lands and vineyards."

So Nehemiah went to the mortgage holders and told them their security was in jeopardy, whereupon they supplied men and money to build the walls and gates. The surrounding tribes tried to prevent this and Nehemiah had to provide soldiers to protect the workers as they labored.

"And the Horonites, Ammonites, Ashdodites and Arabians were very wroth. So from that time forth half of the men wrought and the other half held spears, shields and bows and every builder had his sword girded by his side."

Finally these improvements were completed and Nehemiah had a heart to heart talk with the mortgage men. He said they shouldn't pick on those poor Jews that way. They shouldn't charge so much interest and they shouldn't foreclose so fast. In fact he set up a sort of redemption system which would give relief to the harassed borrowers. Says he:

"I was very angry and I rebuked the nobles and the rulers and said unto them, ye enact usury every one of his brother, and I set a great assembly against them. Then said they, we will restore their lands, their vineyards, their olive yards and their houses. Then I called the priests and took an oath of them that they should do according to this promise. And all the congregation said Amen."

So endeth the story of Nehemiah and the Mortgages.

—*McCune Gill, President, Title Insurance Corporation of St. Louis*

>> AVAILABLE TO YOU: These MBA Certificate of Merit award works in booklet form to members without charge—

Project Construction Financing by George Robert Monroe, Secretary, The Monarch Investment Company, Wichita.

The Mortgage Banker of Yesterday and Today by G. J. Hoffmann, Jr., Treasurer, Stockton, Whatley, Davin & Company, Jacksonville, Florida.

The Motel Story by Jerry B. Frey, Jr., The Brown-Frey Mortgage Company, Dallas.

Simplified Mortgage Service Accounting Procedures by John K. Benoit, Equitable Life Insurance Company of Iowa.

Subdivision Development and Financing by J. Wray Murray, Commonwealth Life Insurance Co., Louisville.

Direct Placement of Industrial Securities by Mortgage Bankers by Walter Mahlstedt, Teachers Insurance and Annuity Association of America.

Mortgage Loan Analysis of Retail Properties by Robert P. Russell, T. J. Bettes Company, Houston.

Auditing the Loan Correspondent by D. R. Olson, Equitable Life Insurance Company of Iowa, Des Moines.

Big Opportunity for Banks Today in Mortgage Credit

Strike While Iron Is Hot says Daniel W. Hogan, Jr.

Get in and develop your mortgage loan department, Mr. Hogan told bankers at ABA's National Credit Conference. It's profitable, the political aspects of home financing are waning, the use of the insured loan is limited at the present and the conventional loan of today is a better loan than it ever was before, he said. Mr. Hogan is president of the Savings and Mortgage Division, American Bankers Association

NEVER has mortgage lending been more in the limelight than now, and never has the banker had within his grasp such a sturdy tool for building up his bank. Never has he had a more exciting opportunity to attract customers, to have an impact on his community, to ring the bell for free enterprise and chartered banking, to vitalize the mortgage function of his financial department store, to lock in an income structure which will pay off for years to come and, above all, to sell Mr. Average Man on the idea that the smart thing to do is to dial "B" for banking.

Yes, mortgage lending is today's big opportunity for banks.

A bold statement, but we've got the facts to back it up. They are:

» Today's heavy demand for mortgage credit is healthy from a credit standpoint.

» Mortgage lending is profitable in the present market.

» The political aspects of home finance are waning.

» Use of the insured mortgage is currently limited.

» The conventional loan has improved in the last 20 years.

» Savings and mortgages go together.

Demand for mortgage credit has reached an astonishing level but only a few years back the average banker was beating his brains out to bring in new income. Operating costs were going up, taxes were already fantastic, volume was increasing, plant expansion was desperately needed, it was taking pay raises to maintain an efficient staff, and money had to be spent on promotion to meet keen competition.

Now it's so easy! We can get all the loans we want—and then some! Practically all American banks are in the same boat. It's a new experience —but a pleasant one. We've got something that people want very much—money! Loans can be made a little more selective.

A tremendous volume of savings is going into mortgages. But, even so, mortgage loans must compete not only with commercial and instalment paper but also with bonds. It's simply a matter of the willingness of mortgage applicants to pay what money is actually worth on the present long-term money market.

Some builders are at last beginning to realize that low down-payments and long terms aren't what they're cracked up to be and that actually they're bad for the borrower and the builder in the long run.

And when is the government going to stop kidding itself and the veterans? Any schoolboy can figure out how much a veteran would save on a $15,000 loan if he could put his hands on a 20 per cent down-payment and if he'd take a 20-year conventional loan at ½ per cent higher interest. Actually the young veteran would be saving $5,355.60 on the financing of his home. Let's help him save it!

There's no question about it, today's heavy demand for mortgage loans is a healthy new look for bankers. Mortgage business is more profitable than ever before, considering the greater safety of mortgages. Here at last is an opportunity to pay a higher rate of interest to savings depositors who have been the forgotten men for so many years.

Second, mortgage lending is more profitable than it has been for a long time.

For a good many years now, we've been curiously eyeing the greener grass in the other fellow's yard; we've been envying the earnings of savings and loan associations, even though we fully realize that their formula is to invest 92 per cent of their savings share capital in mortgages, and mostly in conventional mortgages at that. It's no secret that banks can't legally lend more than 60 per cent of time deposits in mortgages. That's the way we want to keep it, because there's a

whale of a difference between banks and loan associations.

But let's not drown ourselves in our own liquidity! Here we are in the middle of a once-in-a-lifetime opportunity to build up some real capital structure out of a flourishing mortgage business. Don't let it slip through our fingers.

In a good many well managed banks, it's the mortgage department that furnishes bread-and-butter earnings without fuss or feathers to carry the load, year after year. But a number of banks still have a bad hangover from a tragic mortgage binge of many years ago; they're living in the past, and even today, they won't touch a mortgage loan with a ten-foot pole.

That's too bad. Actually, banks have a big stake in the mortgage business. In fact, in 1956 banks alone held mortgages to the tune of $40 billion—and that ain't hay!

It's high time that those banks which have soft-pedaled mortgage lending all these years realize that an aggressive mortgage department can bring home the bacon just as well as any other department that's on the ball. Furthermore, the mortgage customer who likes doing business with his bank is a live prospect for a safe deposit box, an appliance loan, and a savings account.

Even a bank whose commercial loan rates are just as high as its mortgage rates should still make mortgage loans, because it has a duty to its community—and it shouldn't want to stimulate direct lending on the part of the Federal Government.

Third, just why are the political aspects of home finance on the wane?

It's primarily because of the way people at the grass roots are thinking and voting these days. People back home are sick of being constantly muddled up in the crazy schemes of socialistic planners whose two feet are invariably planted firmly on thin air. They're tired of having to foot the bill.

When the Federal Government first entered the housing field 24 years ago, it was to put out a fire—but we didn't expect the fireman to stay for dinner. But he did, and he's still got his feet under the table. Sometimes measures adopted to meet an emergency turn out to be a political football, and the result is a complicated network of rules and regulations which are hard to shake off. Such has been the case of housing and home finance. At last, nature seems to be taking care of the situation, and government influence is dwindling.

The fact that banks are making proper use of the insured mortgage, the fact that the conventional mortgage is coming into its own, and the fact that the Voluntary Home Mortgage Credit Program is working out so well all tend to minimize government activity in home finance and to discourage direct lending on the part of government.

Yes, politics in home finance is at the lowest ebb in many years, and we only hope that a sane administration and a conservative Congress, each wearing a different party label, will keep it that way.

Fourth, it's hard to believe that today the insured and the guaranteed mortgages are giving ground as lending mechanisms. But it's true. And strange as it may seem, their decline in popularity is not entirely due to unrealistic, fixed interest rates, even though there was a good deal of beefing during 1956, until the rate situation was partially corrected last December.

To understand the present situation accurately, turn back to 1933 when the HOLC Act was passed. Many a bank had gone through the wringer and many were still licking their wounds as a result of a beating they'd taken in "tintype" mortgage loans. Some bankers solemnly swore never to make another mortgage loan—and some haven't.

As for the HOLC, it did a "super-duper" job bailing out borrowers and lenders; it left its mark and then passed out of the picture.

Left behind was FHA, which appeared on the scene in 1934 to set a new pattern for mortgage lending. The original purpose of FHA was to prime the pump, to entice reluctant lenders back in the mortgage business. By spreading the risk of mortgage financing, FHA was devised as an emergency measure to help people who couldn't otherwise own their own homes.

Then the VA mortgage came along to help the veteran get preferential treatment. He got it, in a big way, and every one was satisfied.

There was no thought of making FHA or VA permanent, no thought that the government would eventually presume that every family deserved a fine home whether it could afford it or not, and certainly no thought that the banker might go overboard and rely solely on Uncle Sam. Yet all of these things have been taking place.

Most bankers are getting pretty fed up with vanishing down-payments, with terms that look like a geological epoch, with phoney discounts and charges to enhance yield, and with deeper and deeper encroachment of government in the mortgage field.

The pendulum is swinging the other way. But be that as it may, let's give credit where credit is due. Let's not overlook the true facts about FHA which has turned in a tiptop pay record. FHA has drawn up the specifications for a broad, volume market. It has paved the way for the modern conventional loan. It still has a legitimate place in a bank's lending activity, because worthy loans can't always make the conventional mortgage grade.

Bankers can thank their lucky stars that the conditions which originally brought about FHA no longer exist. We can pat ourselves on the back that we've found another more profitable way, a way that virtually makes it unnecessary to resort to mortgage insurance.

Fifth, bankers have at last developed a topnotch conventional mortgage. In the old days, the conventional loan was a Model T. To be brutally frank, the old-style conventional mortgage was a pretty sorry loan for the borrower and the lender. Because it took a 50 per cent down-payment to buy a home in those days, a man and his wife were generally middle-aged before they could afford such a luxury. Then, too, it wasn't easy to scrape up the large interest and principal payments which fell due each six months.

But the modern conventional mortgage is a horse of a different color. In fact, it's turned out to be a pretty good loan as to amortization, terms, appraisals and loan values. It can be easily tailored to fit the individual needs of the home purchaser. Interest rates are flexible; they don't ignore the fundamental law of supply

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NEEDED NOW MORE THAN EVER: A REAL SECONDARY MORTGAGE MARKET FACILITY

WHAT IS A secondary mortgage market, do we have one at the present time? Do we really want a secondary market and, if so, could a secondary market be made to function under existing conditions?

To get the answers, we encounter a confusion in terms. In the parlance of the trade, the secondary market is the source of funds created by the savings institutions that acquire their mortgage investments from mortgage originating companies and ordinarily depend upon these companies for the servicing of the mortgages so acquired. According to this view, the life insurance companies are the main participants in the secondary market. The large eastern and northeastern mutual savings banks also figure prominently in this concept of a secondary market.

Actually the institutions referred to are "secondary" only in the sense that they invest through intermediaries. The market they provide is a limited one. They ordinarily invest only through a more or less fixed group of intermediaries and are not open to all comers. Moreover, they are not "in the market," as the saying is, at all times or under all circumstances, or for all types of mortgages —not even for all varieties of insured or guaranteed mortgages.

Furthermore, with a few outstanding exceptions, the intermediary institutions, which originate and service the mortgages, cannot be considered to provide a true "primary" market, since they generally do not originate mortgages except on what in effect are orders from the secondary institutions or in the pretty clear prospect of receiving allocations of funds from them. Few of the intermediary organizations use their own funds extensively for the original acquisition of mortgages or obtain bank funds for this purpose except on the strength of a "firm take-out" or commitment from a secondary institution to acquire the mortgages within a specified time.

In a real sense, therefore, the so-called secondary market is the primary market. Its attitudes and policies determine the amount of mortgage origination that takes place, while the originating companies act more frequently as agents than as prime movers.

A year or so ago, when the sources of ultimate mortgage money gave the illusion of inexhaustability, something of a different sort began to develop. Many mortgage companies, on the basis of open lines of credit or other arrangements with commercial banks, originated mortgages without positive "take-out" commitments and then warehoused the paper, pending its ultimate disposition. Some insurance companies and savings banks also used a similar medium—the sale to commercial banks under a repurchase agreement—to help them out of the embarrassment of temporary over-commitment.

In engaging in these activities, the commercial banks were actually providing a source of interim or secondary credit, if not an actual secondary mortgage market. But, as such, it was not organized with clearly defined purposes; and, in the final analysis, it served the purpose of expan-

***By* MILES L. COLEAN**

What we think of now as the secondary market is, says Mr. Colean, the primary market. Its attitudes and policies determine the amount of mortgage origination that takes places, while the originating companies act more frequently as agents than as prime movers. A great deal of thinking, discussion, planning and legislation have occurred during the past two decades but we still do not have the kind of instrument which, it appears, the industry ought to have. Mr. Colean gives here, as he did at the MBA-NYU Senior Executives Conference, the history of the various efforts in this field—and makes some recommendations of his own.

sion better than it did that of stability. With the decreasing availability and increasing cost of bank credit and with the discovery that ultimate sources had an unexpected quality of contractability, these practices have been recognized as both hazardous and impractical, if not impossible, as a continuing method of expanding business.

At the present time, the problem of mortgage companies by and large is to work their way out of—rather than into—warehousing arrangements. I know only of isolated instances where sources of such credit have been sufficiently well established for a sufficiently long period ahead to warrant an originating company to proceed on its own initiative, that is, without a specific commitment.

Another aspect of the present mortgage market deserves mention, namely, that mortgages once placed in the hands of an investor such as an insurance company or a savings bank rarely reappear in the market. Such an investor is truly an ultimate one. The mortgages he holds are relatively illiquid, for there is no place he can assuredly go in case he should have the desire, or face the necessity, of reducing his portfolio. In other words, for such institutions there is no reserve or secondary outlet.

These questions of the need for and purposes of a secondary mortgage market were thoughtfully studied in 1953 by a subcommittee of the President's Advisory Committee on Government Housing Policies and Programs. This sub-committee concluded that there was a place for a facility which, through buying and selling insured or guaranteed mortgages (it recognized the impediments to such dealing in conventional mortgages), could help to even out the peaks and valleys in the availability of mortgage funds and hence provide a more continuous flow of activity, with particular reference to the parts of the country that are remote from the main centers of capital supply.

The subcommittee recognized that the final and only true source of funds for mortgage investment was in the savings of the people, and it did not presume to concoct a facility that would create an additional supply of funds through a continuous and expanding use of bank credit. In short, it looked upon the function of the contemplated facility as one of aiding in the distribution of savings, area-wise, rather than compensation for real or supposed shortages in the supply of savings in an attempt to maintain some hypothetically desirable level of activity. The subcommittee considered even this limited function to be feasible only if interest rates were in tune with the market and if there was sufficient penalty for using the facility to discourage resort to it except in necessitous situations.

The limited function of a secondary facility as defined by the subcommittee does not, however, satisfy everyone. It does not satisfy many builders who consider ample credit for building, irrespective of conditions elsewhere in the economy, to be the one requirement for a continuous market. It also does not satisfy those whose disposition is toward state planning and the subordination of market forces to officially determine social priorities. All of these stress the function of market support to assure the maintenance of a preordained interest rate or of a stable or even a rising level of activity in a time of a restriction in the normal supply of funds.

In other words, what these people want is a supplemental primary mortgage market and not a secondary mortgage market.

The confusion in the meaning of "primary" and "secondary," as applied to mortgage markets is also present in dealing with the Federal National Mortgage Association. As initially conceived and as provided for in the original National Housing Act, national mortgage associations were clearly intended to offer a new medium for channelling savings into mortgage investment. There is no question but that they were intended to create a new kind of primary market. At that time there was a severe breakdown in the flow of funds from the customary sources and there was a considerable hoarding of currency. It was felt that a bright new instrumentality carrying the prestige of the federal government would draw forth funds not otherwise available.

> ***"I urge that a group consisting of representatives of MBA, the Life Insurance Association, the American Bankers Association, and the Investment Bankers Association be created for the purpose of taking on this job (of creating a secondary mortgage market facility). I would also urge that a group so constituted dedicate itself to the proposition that the solution should be found within the resources of our private financial system. In other words, I urge that the private interests involved seek strictly a private answer. I do not hesitate to put my proposal as I do because I am convinced that there is no other way of reaching a satisfactory answer. Any other point of departure involves the financial participation of government and hence the control of policy by political forces."***

When the Federal National Mortgage Association was formed in 1938, it was with this concept in view; and FNMA **did** act for several years as a source of funds supplementing those of the still reluctant savings institutions. But there was one important divergence from the original idea: instead of tapping savings, by issuing long term obligations to the public, FNMA issued short term notes, which were mainly absorbed by the banking system. In other words, FNMA was providing a **primary** rather than a secondary market; but it was doing this not with savings but with bank credit.

As the war came on, a surplus of savings for investment in home mort-

gages developed out of rising income and the curtailment of the normal outlets for spending. FNMA took advantage of this situation to liquidate a major part of its holdings. Thus, at this point, FNMA was able, quite fortuitously, to give at least the appearance of operating a secondary market. Out of this experience the idea began to evolve that the appropriate functions of FNMA were not to offer a source of funds in addition to those ordinarily obtainable from institutional lenders but to buy in periods of either general or local stringencies of funds, to sell promptly as opportunities were afforded, to clean up congestions that might develop from over-commitment, to provide a source of liquidity for private institutions, and hence to help assure a steady availability of funds and a stable volume of lending and building activity.

These functions certainly are those of a true secondary market facility. They roughly conform to those contemplated by the President's Committee. They were at least implicitly embodied in the FNMA as reincarnated in the Housing Act of 1954, after some sensational postwar vicissitudes as a private lender.

It has taken only a short time to develop a striking discrepancy between principle and practice. This discrepancy probably, in part at least, was due to the appearance of a situation that was hardly foreseeable by those who had been psychologically conditioned by a long period, only briefly interrupted, of easy money. Instead of a continuation of easy money something showed up that looked like a chronic excess of demand for long term credit in relation to the supply of savings. This was not a short term matter easily remedied by the temporary measures which FNMA was equipped to take.

In the FHA-VA mortgage area, the situation was now—that is of late 1955—complicated by two unique factors: one was a large excess of commitments in relation to the actual, as compared with the contemplated, availability of funds; and the other was the fixed interest rate, set a level below what was broadly competitive in the financial market. As a consequence, many institutions were forced to curtail their operations until their commitment-to-growth ratio had been brought into better balance, while institutions generally, faced as they were with an abundance of investment opportunities at higher yields, were disinclined to expand their FHA and VA holdings.

What Policy to Follow?

Under these circumstances, what policy should be followed by a secondary market facility? Theoretically the indicated action would be to relieve the congestion in the market by absorbing some of the surplus commitments, leaving the forces of the market to concentrate on the maintenance of a flow of new mortgage activity. The theory fell down, however, because the rigidity of the interest rate structure prevented the market forces from being operative. Consequently, any relief in the mortgage congestion promised only to provide funds for diversion to other forms of investment where yields were more attractive.

This is the problem with which FNMA was faced this fall. Unable to cope with a congestion which the rate situation constantly made worse, it abandoned—and, in face of a decision not to modify the interest rate, it is fair to say it was forced to abandon—any effort to perform a theoretically appropriate secondary market function and, instead, relapsed into its old role of providing a primary source of funds for a market now starved by a submarket interest rate. In doing so, it left behind the overhang of commitments and unplaced mortgages to work their way out whenever and however they might, and devoted its modest effort to the support of new building. This situation was not much changed when the FHA rate was finally lifted to an inadequate 5 per cent.

It seems probable that, if the interest rate were free to find its own level and if FNMA turned its resources to cleaning up the worst of the existing situation, a more orderly market would be more rapidly restored and new construction would be better served than can now be the case. This, however, is beside the point. Such indirect methods are not well understood either in Congress or in the trade. The preference is likely to continue to be for the policy that is now being pursued, except for more of it. What we actually have, and what many appear to want, is simply a means of avoiding the impact of restrictive monetary policy on this particular sector of the economy.

I have taken a long excursion from the questions I raised at the beginning; but, out of it, I think some answers can be stated. If we consider a secondary market to be a place where credit can be obtained for the purpose of relieving congestion, of providing liquidity, and of evening the flow, but not permanently adding to the total of mortgage funds, then we do not now have such a facility; and we have never had one except in a tentative and incomplete way. What we have had have been methods of permitting, through the use of bank credit, an expansion of mortgage activity beyond what would have been possible from the available supply of savings under conditions of a fixed interest rate.

In view of the present financial situation and the present political configuration, I see no prospect of anything else. The present Congress, with administration support at least part of the way, seems sure to favor a substantial increase in the authority of FNMA for the now well established objective, namely of adding, through an expansion of bank credit, funds for mortgages beyond what may be available from long term investors, especially where the administered interest rates have been miscalculated in respect to the market. And this type of activity, I reemphasize, is not a secondary market at all but a primary market, and an inflationary sort of primary market at that.

Perhaps it is too much to expect anything else. Perhaps the political implications of housebuilding, like those of agriculture, have become too compelling for us to assume that a home mortgage system, developed strictly along free market and private credit lines, would any longer be acceptable. Although I am by no means sanguine about the prospect, I am not yet ready to throw in the sponge. I still think a sound, practicable, and dependable private home mortgage system can be developed.

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Battle to Preserve t

MONEY is tight and the reasons need to be understood. At stake is the protection of the buying power of the dollar. At stake also is the stretching out of the present period of high prosperity and employment.

Fortunately the long future of our economy is one of rich promise. Thanks to technological advance and population increase, the long-term prospects are superb. The wide recognition of this fact leads to the speculative enthusiasm that inspires some of the current plant expansion. These prospects are so full of hope for high employment and an ever-rising scale of living that it would be a pity if they were to be lost through failure to grapple with the immediate problems. These problems stem from the fact that currently aggregate demand is in excess of supply. Prices are being pushed upward, the economy endangered by cost squeezes, and values inflated by speculation. Too often binges have led to painful hang-overs.

At a time when the general business climate is inflationary, it is obviously necessary to pursue credit policies designed to restrain excessive credit expansion. Also it is obviously not feasible for commercial banks to provide for the accommodation of all who wish to borrow. Some loan applications must necessarily be refused or deferred by commercial banks, even though they may be technically creditworthy.

The rise in interest rates, including Federal Reserve bank discount rates, seems to have caused considerable apprehension lest the supply of funds in the money market be insufficient to provide for essential credit needs, such as the movement of crops and the financial requirements of the Federal Treasury. The Federal Reserve System has no intention of allowing such a situation to develop. The Federal Reserve System has the continuing duty of providing a monetary expansion consistent with orderly growth of the economy. The discount facilities of the Federal Reserve banks continue to be available to member banks requiring temporary funds for their essential needs.

The goal of economic progress is more jobs and more goods combined with a dollar of stable buying power. The road toward this goal stretches ahead as an inviting path provided the current economic traffic does not become snarled. Into the road there is now pouring more economic traffic than the present road capacity will permit to move forward at one time. This traffic comes both from government and from private sources; from corporations anxious to expand, and from individuals who wish homes and other durable goods. Too many people wish to get through first even if they disregard the rules of the road.

What is the nature of this traffic jam that threatens to impede economic progress? The demand for scarce goods is exceeding the supply and pushing prices upward. This explains what has been happening with respect to wholsesale and consumer prices.

Too many people want too many things too fast. They want to build new plants, office buildings, ships and planes at an unheard-of-rate and still retain record rates of production for residences and autos. The resultant pyramiding of demand not only creates scarcities such as that for steel and cement, but for certain labor skills as well.

What is so clearly evident in the case of scarce materials and labor applies also to money and credit. The so-called tightness of credit is often attributed to insufficient supply, whereas it has in fact resulted chiefly from a pyramiding of demand. Actually the supply of money and credit is larger than a year ago, instead of being smaller as many imply when they use the phrase "tight money."

Moreover, money is being made to work harder. Demand deposits are being turned over about 8 per cent faster than a year ago. This increase in money activity is to be expected in a period of credit stringency, and has the effect of making the supply of money more efficient.

The aggregate and rival demands of corporations and individuals to borrow heavily in order to buy more goods than exist at the moment explain the concern over the cost and availability of credit. When the demand for credit exceeds the supply of it, the price tends to rise. This is how the marketplace allocates the existing supply of credit among the rival claimants for it. In the process, many individuals and companies are disappointed and they cannot secure the funds to buy what they want right away.

As a nation we are trying to spend faster than we save. If we should succeed, the higher prices that would result spell inflation with all its dread consequences to savings and to those dependent upon them. The well being is involved of wage earners who have pension rights and similar fringe benefits as well as that of widows, school teachers and all whose incomes are fixed.

There are some who would curb spending through price controls and rationing. Such direct or selective controls over imports, food, critical materials and credit were resorted to by many nations, including our own, during and immediately after the war. They are only a partial answer. Even supported by wartime patriotism, their success was limited and in the end did not prevent inflation. They did not prevent eventual loss in the purchasing power of the monetary unit. And they did involve the policing of hundreds of thousands of industrial and commercial enterprises and of private citizens. It is little wonder that country after country shook off this harness of governmental controls when peacetime conditions permitted free markets to operate be-

e the DOLLAR

At year-end, scores of forecasters were predicting that the biggest economic problem of 1957 would be tight money—are present credit policies sound, are they in the public interest, should a halt be called, do we need a complete reexamination of our monetary system? Consensus was that what we are experiencing in the regulation of our credit structure is a necessary aftermath of the busy times we have been living and working through. Now, too many people want too many things too fast. If we want to preserve the purchasing power of the dollar—something every citizen can understand—prosperity and employment must be stretched out. Mr. Balderston, high in the councils of our money managers, states the case for the wisdom of present policies, as he did for members of the National Association of Supervisors of State Banks. He makes a good case for doing what we are doing now.

***By* C. CANBY BALDERSTON**

Vice Chairman, Board of Governors of the Federal Reserve System

cause such markets enable individuals to determine for themselves what they need, what they will buy, and at what price. Even though many individual spending decisions be unwise, the free market gives people the satisfaction of using their own knowledge, judgment, and initiative. In a democratic free-enterprise economy we must depend upon free markets and upon intelligent, not irrational, decisions on the part of businessmen and consumers.

The proper role of government in these matters is to be responsible for fiscal policy, including the balancing of its own budget, and for general monetary policy. Responsible for the fiscal policy are the Treasury and the Congress. Responsibility for monetary policy has been assigned by the Congress to the Federal Reserve System with a mandate to serve as a trustee over the total supply of money and to carry on its work without fear or favor, free from partisan political pressure on the one hand, or private business pressure on the other. Its particular role is to regulate the reserves available to the commercial banks so that bank credit may expand and contract flexibly in accordance with the fluctuating needs of the economy. In the light of the Employment Act of 1946, those needs may be expressed most simply as the fostering of sustained economic growth and the maintenance of economic equilibrium.

There can be no economic equilibrium without stable buying power of the dollar.

If the supply of credit becomes excessive in relation to the goods and services available, prices tend to rise; if the converse is true, prices tend to fall. Therefore, if the value of money is to be stable and to assist the economy to move steadily upward, its supply (at the current rate of deposit turnover) must be harmonized with the flow of goods. Hence, the supervision of government is needed over the total supply of money and credit. The apportionment among individual borrowers, however, is best left to competition between private bor-

rowers and private lenders. It is the responsibility of the central bank to influence the total supply of credit but the selection of the particular customers to whom loans are to be made is left to the discretion of commercial bankers and other lenders.

The problem, then, is to keep the economy running at high speed without overstraining its capacity. A continuous stream of transactions must be kept running much like the stream of traffic on a crowded highway. The latter can move with speed and safety only if drivers observe the traffic rules brought forth by experience.

The rules of the economic road, like traffic rules, are sometimes ignored. Perhaps the most fundamental of them is the preservation of balance and proportion between protection and risk, caution and daring, liquidity and expansion. Moreover, the quality of debt should not be impaired by equity that is overly thin. Finally, the decision-making of lenders and borrowers, whether business executives or consumers, must be prudent to provide economic growth free from serious inflation or from recession with its destruction of values.

The financial panic of 1907 that led to the founding of the Federal Reserve System six years later, the inventory panic of 1920 and 1921 with its crashing prices, and the collapsing stock market of 1929 and 1930 all preach their respective sermons. The quality of past business decisions may be said to determine the fundamental soundness of the economy at any given time. The decisions of 1955 are reflected in the sales inventory, and employment figures of 1956 and may indeed influence those of 1957. These business decisions not only are influenced by group psychology, they help to create it. Sometimes they reflect excessive pessimism; sometimes speculative optimism.

One lesson of the depression of the 1930's would seem to be that if equity values suffer from too great destruction, those executives who must venture if the economy is to revive are too distraught and fearful to do so; or if they have the requisite courage and daring, they may no longer be considered credit-worthy by lenders.

In contrast is the psychology of ebullience and unwarranted optimism. Financial history records boom after boom that burst because men "chased the fast buck" at the sacrifice of prudence. Two observations may be in order. One is that speculative fever may not, if it should again sicken the economy, take the form of stock market speculation like that of 1929 when margin requirements were too low and the rewards of the call-money market were too enticing. Speculation has many forms of dress and even of disguise. The second observation is that neither monetary control nor fiscal policy, nor the two in concert, are likely to maintain economic stability if group psychology runs rampant. How could they revive business from depression in the face of general despair? Or prevent inflation amidst a wave of reckless business decisions?

The problem of protecting the purchasing power of the dollar is like a three-legged stool. It requires the combined action of general monetary policy, of fiscal policy, and of prudent decision making by labor leaders, business executives and consumers. It would be highly desirable for each businessman and consumer to regard himself as a trustee of the economic health of the whole community. A philosophy of trusteeship and a sense of responsibility are salient features of democratic free enterprise.

>> PRUDENCE IS THE WATCHWORD: There is a widespread feeling that the pressures for credit demand are not likely to abate for a long time to come. There may be interruptions now and again, just as there were in the past eight years; but the picture of economic growth that is being painted by the forecasters portends a great need for capital and credit as we look toward the future.

"We have come a long way toward recognizing the importance of flexible monetary actions in preserving economic stability. It has been a long and at times discouraging process—but it seems to be taking hold. Now that we have arrived at a point where credit policy touches the lives of more people more positively and more directly, we bankers should not lose the opportunity to correct false impressions about credit.

"But this is just one facet of the credit picture. As we look at the credit picture in broad perspective, we should realize that much more needs to be done to create a better understanding and smoother functioning of our whole financial structure. Over the past two decades—and particularly in the postwar period—sweeping changes in the relations between various kinds of financial institutions have taken place. It is becoming more apparent almost daily that these changes bear careful study. A decade ago, savings were in great abundance and interest rates were close to an all-time low. Today the situation is reversed. Savings are being outstripped by demand for capital, and interest rates are higher than they have been for some years. A race has developed among financial institutions to obtain those savings and to channel them through their credit facilities. This has conditioned public attitudes toward various institutions and has affected their functions, responsibilities, and policies. There needs to be a clearer understanding of these facts, and the banking industry should be in the forefront in the creation of that understanding."

—Erle Cocke, ABA President at the National Credit Conference

President's Page

A Paradox Of Our Times:

INFLATIONARY AND ANTI-INFLATIONARY IDEAS GROW SIDE BY SIDE

PROBABLY no national budget of this generation has occasioned the thoughtful consideration and study which the American people are giving to the one just submitted by the President. As the largest in peacetime history, it would appear to set a pattern for the immediate future, a pattern which calls for continued heavy spending, little decrease in foreign aid, more big government and—what is disappointing to people generally—no immediate relief from the heavy tax burden.

All of these facts, and implications for the future, are being examined and discussed amid warnings from every government source that our greatest domestic danger today is inflation. Our people are being made more conscious of the threat of inflation than they have ever been in the past—the most conspicuous warning coming in a most tangible way, the continued restraint of credit. Yet, in the government's sincere and commendable effort to dampen the fires of inflation, something else is developing, something as inflationary as anything that could be proposed. And this something touches our area more acutely than almost any other. It is a strange paradox of our times that, on one hand, this nation is making a determined effort to halt inflation and preserve the stability of the dollar yet, on the other hand, some of the most inflationary schemes are being proposed in the national Congress.

John F. Austin, Jr.

Actually, what is being proposed and considered at this moment adds up to the most serious threat we have yet seen to private enterprise in mortgage financing. Direct lending in our field is being discussed as never before. Some of the most influential members of the Senate and House have introduced legislation which would permit substantial portions of the Veterans' National Life Insurance Fund to be used for purchasing GI loans at 4½ per cent. Other bills provide for dropping the down payments for FHA loans drastically. There is by no means a general agreement in the Congress that the GI rate should be increased even though it is plain that, without it, these loans will all but disappear. Rather than face the hard facts indicating the need for flexible interest rates, many members of the Congress persist in looking for other alternatives—and, again, what is significant is that so many of the score or more legislative proposals are being made by highly influential members of the Congress.

As much as we would like to see the GI loan on a stable basis and as much as we would like a greater investor interest in FHA loans, none can deny that a good deal of what has apppeared in these early days of the new Congress are mere palatives, are highly inflationary, and, in all candor, do not serve the best interests of the country.

What has seemed so significant to me these past few weeks is the real threat which these developments pose for our private mortgage financing. Really large-scale direct lending is now more of a possibility than it ever was in the past. It is something to which every mortgage banker should be alert—the possibility has grown considerably beyond the limited VA program of recent years. As I am recording those observations, members of our Executive Committee are preparing to gather to consider these legislative suggestions and I will report on our deliberations.

In the meantime, I am more convinced than ever that the observations which I have made recently at the Chicago, Philadelphia and other local MBA meetings are the correct ones—namely, that, in general, the present credit restraints are necessary, that they may well continue for some time and that it is up to us to learn to live with them.

J. F. Austin Jr.

PRESIDENT

The Least Understood

THE Federal Reserve Bank of New York undertakes a great variety of important activities, most of which are related in some degree to the operations of the Federal Open Market Committee—such things as handling the reserve and borrowing accounts of the members banks, the provision of currency, the processing and crediting of checks received for collection, the expediting of wire transfers of deposit balances among banks and of Government securities among investors, the calling and disbursement of funds for the U. S. Treasury, the handling of transactions for foreign central bank and government accounts representing settlement of the United States balance of payments with other countries, and the supervision of member banks.

These activities, most of which we undertake in common with the 11 other Federal Reserve Banks, have a great deal to do with the System's major responsibility of contributing to an efficient and adequate money and credit mechanism for the nation. But they are some times referred to as "defensive" or "passive" operations, in contrast with the three "dynamic" or "active" instruments—reserve requirements, discount rates, and open market operations—which are employed in our efforts to minimize both inflation and deflation and to facilitate economic growth.

To discuss the Federal Open Market Committee's activities without referring to all three of these instruments would be quite misleading. For while it is true that the Board of Governors alone has the responsibility for determining reserve requirements, and while discount rates are established by the individual Reserve Banks—subject to review and determination by the Board of Governors—in practice the Federal Open Market Committee has become the principal forum in which these two instruments, as well as that of open market operations, are discussed and weighed by representatives of the entire System in arriving at a System-wide consensus as to what should be done at any given time in the field of general credit control. The emergence of the Federal Open Market Committee as the meeting place where representatives of all parts of the System's complex structure can be brought together, for joint discussion of interrelated responsibilities, is one of the most interesting, and also probably one of the most constructive developments in Federal Reserve history.

Meetings of the Federal Open Market Committee are generally held every two or three weeks in Washington. The Committee consists of 12 members, including the seven members of the Board of Governors and five of the Reserve Bank Presidents. The President of the New York Reserve Bank is continuously a member, while the other four Presidents are appointed in rotation. The 12 members of the Committee, which was established by statute, sit and reach decisions as responsible individuals, not as representatives of any constituency. Each must find the answer in the light of all the facts and his own conscience, to the question, "What policy of credit control would be the best policy under present conditions for the economy of the United States?" Naturally each member brings to the Committee the full benefit of any special information available to him, including—in the case of the Reserve Bank Presidents—information concerning economic conditions in the various districts and the views concerning them held by businessmen and others; but each member also gives careful consideration and makes his final judgment on that basis.

The seven Presidents who are not, at the time, members of the Federal Open Market Committee nevertheless attend these meetings regularly by invitation and participate in the discussions on the same basis as the 12 Committee members, with the sole exception that they have no vote on matters requiring a vote. Thus the Committee obtains a first-hand report on conditions in each of the 12 Federal Reserve Districts. During the periods between meetings, the seven Governors and the 12 Presidents are of course pursuing their various other duties, but they are also preparing for the coming deliberations of the Federal Open Market Committee by observing the results of policies established at previous meetings, gathering new economic data, and continually reviewing their judgments of past decisions and current events.

In New York, for example, our senior officers gather at least once each week to review important developments, and we have another special meeting of officers a few days in advance of each Federal Open Market Committee meeting for the special purpose of discussing the current state of business and credit conditions, Treasury finance, and related matters, and what type of credit policy seems best suited to this state of affairs.

At each Federal Open Market Committee meeting the procedure is to have the Manager of the System Account, who is also Vice President in charge of the Securities function at the New York Reserve Bank, lead off with any observations he may wish to make on what has actually happened in the Account and in financial markets in general since the last meeting. He will already have furnished each member of the Board of Governors and each President with special written reports that are complete through the close of business on the preceding day. Thereafter two of the senior staff members of the Board of Governors present a comprehensive and

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Operation in Finance

It's the operation of the Federal Open Market Committee which, relatively speaking, only a handful of people understand. Some people think of it as a mysterious group of people working in New York, exerting a tremendous control over our money and credit. And what some people do not understand, they are likely to view with suspicion. Time was when mortgage men did not have to bother to understand such things as this—but it is to their advantage to do so now. The mortgage market does not stand alone, it is a part of the vast complex scheme of things under the general heading of money and credit. And the Federal Open Market Committee has an important and necessary role in the whole operation. Mr. Hayes undertook to explain just what this Committee is, why it is and how it operates for members of the Sub-committee on Economic Stabilization of the Joint Committee on the Economic Report at their recent hearings. He's succeeded in doing just that; and while, admittedly, it is a bit on the heavy side, the fact remains that here is a vital operation in the field of money and credit that affects us profoundly and thus we ought to understand it.

by **ALFRED HAYES**
President, Federal Feserve Bank of New York

detailed summary of current business and credit conditions in the country as a whole. After this the Chairman, following such introductory remarks as he considers appropriate on domestic or foreign developments, calls on each President and each Governor, in turn, to give his appraisal of the current situation and to state his views concerning appropriate policy in the circumstances. Customarily the President of the New York Reserve Bank is called on first, and, because of the location of the Bank in the country's money center, I usually talk of business and credit developments and expectations in national terms, and of the open market and other Federal Reserve policies I would consider appropriate in the light of those developments. The other Presidents usually start off with comments on conditions in their particular districts and they, too, give their views as to credit policy. Likewise each member of the Board of Governors states his opinion concerning the appropriate policy after discussing any particular developments in the country's economy which appear to him pertinent. Generally the last man to comment is the Chairman of the Federal Open Market Committee, who is of course also Chairman of the Board of Governors. He summarizes this own appraisal of the situation and then undertakes the difficult task of pulling together the threads of all preceding discussion and expressing the consensus of the meeting in terms of, first, how the directive to the New York Bank should be worded, and, second, what specific actions are called for in the way of open market purchases or sales or other credit control measures —perhaps mentioning, for example, the possibility that consideration may be given to discount rate changes by the various Reserve Banks, or to changes in reserve requirements by the Board of Governors.

The Chairman then gives all present a chance to state whether they agree with his understanding of the consensus. The Manager of the System Account is asked whether the instructions are sufficiently explicit to enable him to carry out the Committee's wishes effectively, and at this point the Committee has an opportunity to convey to the Manager any nuances of policy which they think should be kept in mind.

I have been greatly impressed by the effectiveness of this whole procedure in bringing together a variety of disinterested and objective views on our country's economic conditions and problems, and then by deriving from these a reasoned consensus as to monetary and credit policy. Often the opinion of any one member is not yet crystallized when he arrives at the meeting, and it may well be modified during the meeting by his process of give-and-take. On the other hand, I think it is pretty clear that with 19 well-informed people having a full opportunity to present their views, on the basis of data assembled by able staffs throughout the System, it would be quite impossible for any one man holding an extreme position to dominate the Committee and dictate the

Committee's conclusions. Indeed, the thinking of any one man may not be fully in accord with the consensus; the consensus is acceptable because it is a fusing of all the views, and it provides a workable basis for operations. Over time, such a consensus is bound to be far more reliable than the occasional flash of insight that a single individual might produce.

I have been struck by the degree of harmony which has been achieved in this whole procedure. It has almost always been possible, without even the formality of a vote, to reach a consensus through the give-and-take of reasoned discussions.

The general conclusions of the Committee as to credit policy are set forth in the directive issued to the Federal Reserve Bank of New York. The directive is amplified by the statement of the consensus and by the full discussion, all of which are of course noted in the Committee's minutes. From this point on, and until the next Federal Open Market Committee meeting, the primary responsibility for conducting open market operations is in the hands of the Federal Reserve Bank of New York, acting in accordance with the instructions of the Committee. With the country's money market and securities markets centered in New York, most open market operations must necessarily be executed there, but the New York Bank is acting at all times for the System as a whole on the instructions of the Committee and is at all times responsive to the Committee's wishes. In my capacity as a member and Vice-Chairman of Federal Open Market Committee, I am in a position to help interpret the Committee's wishes to the Manager, and he himself has of course been present at the last meeting when he was specifically instructed on the varied detailed considerations which the Committee wishes him to keep in mind. He knows, for example, approximately that member bank reserve position the Committee believes appropriate, or he may have been told to give only secondary consideration to this factor and for a time to be guided primarily by such factors as the tightness of the banking structure in the money centers, the degree of market pressure suggested by U. S. Treasury bill rates and other money market rates, the impact of a large Treasury borrowing operation, and even more broadly by that on-the-spot appraisal of current attitudes and actions which is described as the "feel" of the market.

A comprehensive procedure has been worked out for keeping the Board of Governors and the other members of the Federal Open Market Committee promptly and fully informed on market conditions and all actual transactions for the System Account, as well as on contemplated transactions. One of the most effective tools to this end is the so-called daily conference call at 11 a.m., each business day, when the Manager of the Account or his assistant talks by telephone with the Economic Adviser and a senior economist of the Board of Governors. The Presidents of those Federal Reserve Banks outside of New York who are currently serving on the Committee also participate by long-distance telephone in these discussions on a rotating basis, one President sharing in the call for a period of two or three weeks. At the New York Reserve Bank, the First Vice President or I often "sit in" on the telephone call and many times both of us are present. (The First Vice President is, in conformity with the statute, my alternate as a member of the Federal Open Market Committee.)

The Manager of the Account summarizes conditions in the money and capital markets, the various reports or comments received from the dealers in U. S. Government securities, the reserve position of the principal New York banks, and the reserve position of the country's member banks as a whole—together with the New York Reserve Bank's expectations as to changes in this national reserve position day by day for the next few weeks. The Manager then indicates whether these available data and expected developments point to a need for open market operations in order to fulfill the Federal Open Market Committee's instructions—i.e., whether Treasury bills should be purchased or sold, whether re-purchase agreements should be made with dealers, whether holdings of acceptances should be increased or run down, and in approximately what amount any or all of these might be considered.

Participation in the call provides the Economic Adviser to the Board of Governors and the other President who is taking part in the call, the opportunity and responsibility of contributing their views as to existing conditions and the proposed course of action, particularly as these relate to the policy set at the most recent Fed-

> *"It is through the complex interrelations of this network of short-term financial transactions that the money system is kept working smoothly, from day to day, meeting the vast payments requirements of a vigorous, growing economy. The great bulk of the enormous movement of funds through the banking system each day works itself out through an offsetting of funds available against funds required on a local or regional basis, but a net residual of available funds or need for funds remains. It is in absorbing or supplying these residual funds that the central New York money market is of crucial importance. And it is here that the net dependence of the entire financial structure upon the Federal Reserve is brought most clearly into focus. That is why the operations of the arm of the System located in New York necessarily fill a central role in exerting the marginal degree of easing or restraining influence that is needed, if monetary policy is to exert a determining marginal force upon the availability of money and credit for the country as a whole."*

eral Open Market Committee meeting. Usually there is immediate agreement, but suggestions may be made which result in some modification of the Manager's program. Immediately following this conversation, a full summary is prepared to all of the Governors in Washington; the same summary is sent by wire to the various Reserve Bank Presidents.

The staff of the Board of Governors is advised periodically during the day by telephone on all details concerning actual operations and market developments. In addition, a written report is submitted daily to the Board of Governors by the New York Reserve Bank with copies to the interested officers of the other Federal Reserve Banks and branches.

At the end of each statement week a full written report is submitted by the Manager to the members of the Federal Open Market Committee and to the other Presidents. These reports not only provide a complete statement of all actions taken but they also give a full running record of conditions in the money and capital markets, with emphasis on interset rate changes and on the behavior of U. S. Government and other security prices. Prior to each Federal Open Market Committee meeting, a detailed recapitulation of all major market developments and all transactions since the last previous meeting is prepared for submission to all Committee members and the other Presidents.

Questions may occur to the Account Manager between Federal Open Market Committee meetings, perhaps as a result of some unforeseen development at home or abroad, which appear to call for an interpretation of some policy decision reached at the last meeting. If it is a minor matter, the question may be settled by discussion with the President or First Vice President of the New York Bank, but if it involves a major policy consideration, we may decide to consult by telephone with the Chairman, or, in his absence, with the Vice Chairman of the Board of Governors or some other member of the Committee. Or the initiative may come from Washington, i.e., Chairman Martin or Vice Chairman Balderston may telephone me and raise some question or make some suggestion having to do with interpretation of the current Federal Open Market Committee policy. If very urgent questions arise, it is possible to arrange on short notice for a telephone meeting of the Federal Open Market Committee to deal with whatever emergency may exist.

We in the New York Reserve Bank encourage the Governors and the other Reserve Bank Presidents, as well as senior members of the staffs of the Board of Governors and of the other Reserve banks, to spend as much time as they can spare visiting our Trading Desk, observing the Manager and his assistants carry out open market operations, and familiarizing themselves with the actual market atmosphere in which these operations are conducted.

The chief point which I would like to emphasize is the high degree of close contact and close cooperation existing between the Federal Open Market Committee as the originator of all open market policy and the Federal Reserve Bank of New York as the executor of this policy.

I have already touched upon the importance of the New York money and capital markets, which is the basic reason for placing the responsibility for execution of the Federal Open Market Committee's policies on the Federal Reserve Bank of New York. Perhaps it would be useful at this point to explain briefly just what is meant by the nation's "money market" and how the New York Reserve Bank's Trading Desk is organized to keep in intimate touch with that market.

The money market has been defined as the active market for money and close money substitutes which financial institutions and others rely upon to provide the liquidity needed in the usual course of their operations. Commercial banks, Government securities dealers, investment bankers, other financial institutions, non-financial corporations, state and municipal governments, and others turn to the money market to adjust their cash positions—supplying funds when they hold surplus cash, withdrawing or borrowing funds when they need cash. The instruments employed (in addition to bank borrowing at the Federal Reserve Banks) might be short-term Government securities, marketable private short-term paper, demand loans, or "Federal funds"—money that is good at the Federal Reserve Banks today, purchased with money that will not be collected funds until tomorrow.

The money market through which all these day-to-day cash adjustments are made is national in scope, but the residual shortages or surpluses of funds come to focus in New York at the large New York banks. The extensive correspondent and customer relationships of these banks, and the purchase and sale of money market securities by the specialized dealer firms located in New York, provide facilities upon which all other regions depend to settle their shortages or use their excesses.

By providing a mechanism whereby interest earning investments may be converted readily into cash, and short-term money needs can be met through borrowing, the money market provides a degree of liquidity to debt instruments and a degree of flexibility to investment and borrowing practices that are essential to the functioning and the growth of a highly developed industrial and financial system. The participants in the money market are as varied as the economy itself. Business corporations are important and may come to the money market with

temporary cash accruals to invest in short-term Treasury securities, bankers' acceptances, sales finance company paper, or other instruments. The corporations have to be confident of a market for their investments so that the latter can be liquidated readily when these funds are needed to pay dividends or taxes, or for operating purposes. Confidence in the liquidity of their investments has made it possible for them to make money available to others seeking money rather than holding these funds in idle cash balances. A State or local government may have funds from tax collections or from the sale of a bond issue that are not immediately needed and are temporarily available for investment. Foreign central banks may have accrued dollar reserves that may be invested in Treasury bills or bankers' acceptances. All of the financial intermediaries—life insurance companis, such Government agencies as the Federal Intermediate Credit Banks or the Federal Home Loan Banks, or any others—participate in the money market at least some of the time either as borrowers or lenders of short-term funds.

Of course, the 14,000 commercial banks in the United States, or a considerable number among them, are the principal participants in the money market. The deposits held with them are check-book money and may be withdrawn without notice. It is particularly important, therefore, that commercial banks hold adequate secondary reserves in the form of liquid short-term investments to provide a potential source of cash to meet withdrawals. Moreover, commercial banks are required by law to keep minimum cash reserves against deposits; in the case of Federal Reserve member banks, these reserves must be kept with the Reserve Banks. Since cash reserves earn no return, it is in a bank's interest to limit its cash reserves as nearly as possible to the amount required by law. In doing so, however, constant recourse to the money market is necessary, either to borrow money or to sell short-term investments when an excess of withdrawals over deposits pulls money away or to lend or invest short-term funds if an excess of deposits over withdrawals temporarily provides excess cash.

It is through the complex interrelations of this network of short-term financial transactions that the money system is kept working smoothly, from day to day, meeting the vast payments requirements of a vigorous, growing economy. The great bulk of the enormous movement of funds through the banking system each day works itself out through an offsetting of funds available against funds required on a local or regional basis, but a net residual of available funds or need for funds remains. It is in absorbing or supplying these residual funds that the central New York money market is of crucial importance. And it is here that the net dependence of the entire financial structure upon the Federal Reserve is brought most clearly into focus. That is why the operations of the arm of the System located in New York necessarily fill a central role in exerting the marginal degree of easing or restraining influence that is needed, if monetary policy is to exert a determining marginal force upon the availability of money and credit for the country as a whole.

These operations in New York include, of course, a host of varied functions that are also being performed by the System's 35 other arms—the 11 other Federal Reserve Banks, and the 24 Federal Reserve Bank branches, located throughout the country. They include, notably, the discount mechanism through which banks may borrow directly to meet short-run adverse swings in their reserve positions. That is a vast subject in itself. The only special significance of New York in this zone of System activity is that so much of the borrowing need that converges on the large New York City banks results from the residual of pressures exerted on these banks by their correspondents everywhere.

What is more or less unique in New York is the location there of the active center of the trading market in United States Government securities. Because all banks and others may turn to purchase or sale of government securities, as the first line of defense for employing or obtaining money market funds, that market becomes a major zone for the exercise of System responsibility at its own initiative. By buying or selling short-term government securities, or by advancing funds at times to the dealers who are continuously making markets in these securities for all classes of investors, the Federal Reserve can bring about the general degree of tightness or ease that is most likely to fulfill the broad "dynamic" aims of monetary and credit policy.

> *"The piecing together and interpretation of the bits and pieces of statistical data, market reports, development in psychology and news items that goes on constantly in the Securities Department of the Federal Reserve Bank of New York is directed toward a single purpose—the execution of the policy instructions of the Federal Open Market Committee. By 11 o'clock on most mornings enough of the over-all picture will have been assembled to give a reasonably clear idea of the action, if any, that will be called for. From that point on, subject to any questions that may come in from the members of the Committee or their staffs, the job becomes the highly specialized technical operation of choosing the right methods, and the right time, to effect the marginal degree of influence upon the volume of bank reserves, and the state of the money market, that will best carry through the general aims of System policy."*

Here, very briefly, is an outline of the procedures followed by our own Trading Desk, in carrying through each day the instructions of the Federal Open Market Committee. Perhaps I should note parenthetically

that our use of the term "Trading Desk" does not imply that we "trade" in the usual sense—with a view to making profits. Our Desk is, in reality, a listening post and a "transactions desk" where orders are executed.

How the Desk Works

This Desk at the Federal Reserve Bank of New York maintains direct telephone lines with the principal dealer firms and with the commercial banks in New York and Chicago that have Government securities dealer departments. A group of specialists on the Desk are in constant communication with these firms, which are in turn in touch with banks and other investors all over the country, and the composite picture that evolves hour by hour from these conversations and from direct reports from the principal New York banks will show the balance of forces that is taking shape in the money market. Price and yield quotations from various dealers for all Government securities and United States agency issues, the latest Federal funds rate, over-all changes in stock prices, and other information are chalked up on a large quotation board to provide statistical background for the reports and comments that are constantly pouring in. In a real sense, the Trading Desk is the Federal Reserve System's listening post in the money market as well as its operating arm.

Achieving Coordination

Discussions at meetings of the Open Market Committee with respect to its instructions to the Federal Reserve Bank of New York usually include among other things reference to the degree of pressure—ease or tightness—that the Committee wishes to maintain in the money market in pursuit of its broad policy objectives. The discussion may sometimes include mention of targets in terms of bank reserve positions or short-term interest rates that would be generally appropriate to the current phase of credit policy. But it is recognized that statistical measures are not always satisfactory guides to the condition of money and credit availability which the Committee wishes to maintain and that the "feel" of the market, as interpreted by specialists, must be the principal day-to-day guide—that is, the things that close observation can reveal from the standpoint of timing of operations.

I would not wish to leave the impression that the open market operations for the Federal Reserve System are guided largely by educated intuition. Back of the day-to-day decisions to buy or sell Government securities or to enter into repurchase agreements with dealers lies an intensive evaluation of the supply and distribution of bank reserves and of the forces that are likely to influence the money market currently and in the near future. A group of money market specialists works constantly at forecasting the additions to or withdrawals of funds from the national money market which may be expected on the basis of patterns previously observed in changes occurring during a week, month, season or year. Estimates are made of the daily flow of Treasury receipts and expenditures to determine if the Treasury will be supplying or withdrawing funds from the market. Other specialists keep records of scheduled security flotations by corporations and government bodies, including the Federal Government, and the expected influence of these operations on interest rates and market conditions is included in the total picture. Detailed data are compiled on the positions of the New York banks, including their borrowing from the Reserve Bank and in the Federal funds market. And many other statistics and reports are poured into the hopper each day to form part of the background against which operating decisions are made.

The Overall Impression

The piecing together and interpretation of the bits and pieces of statistical data, market reports, development in psychology and news items that goes on constantly in the Securities Department of the Federal Reserve Bank of New York is directed toward a single purpose—the execution of the policy instructions of the Federal Open Market Committee. By 11 o'clock on most mornings enough of the over-all picture will have been assembled to give a reasonably clear idea of the action, if any, that will be called for, and it is then that the conference telephone call—to which I referred earlier—is made From that point on, subject to any questions that may come in from the members of the Committee or their staffs, the job becomes the highly specialized technical operation of choosing the right methods, and the right time, to effect the marginal degree of influence upon the volume of bank reserves, and the state of the money market, that will best carry through the general aims of System policy.

PEOPLE AND

People are increasing all the time which may or ma

THE relationship between population change and the economy of tomorrow has two important aspects: ›› First, there are the changes which have already taken place. The birth rate has behaved like a roller coaster in recent decades. Then, there is the more interesting and demanding task of projecting the population changes which may or may not take place in the future.

Regarding births during the last 35 years, the downward trend of the twenties was accentuated by the depression, then there was some recovery during the war years, and in the past 10 years we have witnessed a boom of tremendous proportions, both in absolute and relative terms. It is interesting to note also that the most recent five years actually show an advance over the more immediate postwar period.

This is another look at population trends, birth rate, and all the economic problems which the turn of events in these departments create. Mr. Fuchs is no dissenter, but can't go along with the forecasts of many visualizing an expanding economy if for no other reason than there are more and more of us to create and enjoy prosperity. He is Associate Professor of Economics, School of General Studies, Columbia University, and addressed Dean's Day at NYU.

What do these figures tell us about the future? First, they give businessmen some idea of the size of the potential market at various stages of life. If your product is needed by babies and young children, you probably are riding the crest of the biggest boom in history. If the teen-agers are your market, you can look forward to some wonderful business in the decade ahead. The figures show us why the marriage rate has been falling in recent years, and why it is likely to continue to be low for several more years. Looking still further ahead, we can see the basis for another tremendous housing boom in the 1970's.

As parents and citizens, the figures may shock us into realizing that an educational plant and staff geared to the demands of recent years will be woefully inadequate to cope with what lies ahead. The schools are already overcrowded, but it is easy to see that the full brunt of the recent population upsurge has not yet made its impact. In order to meet the coming need for teachers, for example, 50 per cent of all college graduates in the next 10 years would have to enter teaching. The average rate in recent years has been less than 20 per cent. Given continued high employment and demand in the private sector of our economy, it is difficult to see how we can avoid a serious deterioration in educational standards. That this may have serious consequences for the economy of the "day after tomorrow" is an ominous, if not obvious conclusion.

What will the birth rate be like in the years ahead?

Most recent discussions of the economy of tomorrow usually begin with the assertion that the high birth rate of recent years will continue. This is often stated almost as an article of faith and not open to question. More cautious souls fall back on reference to the Census Bureau projections, which, one must realize, are merely

PROSPERITY

By VICTOR R. FUCHS

not mean that prosperity increases proportionately

exercises in arithmetic. Very rarely do you see any theoretical discussion of why the birth rate has been so high in recent years, or any attempt to weigh the factors which may bring about changes in the birth rate. But it is precisely such considerations which must enter if you are going to make predictions about future population change. Neither statements of faith, nor mechanical projections with all assumptions stated but on preference among assumptions indicated, are satisfactory.

It is my belief that the birth rate will turn down shortly, and that the population of the United States will not continue to increase at as fast a rate as in the past 10 years, nor will it be as large in 1975 as the typical optimistic speechmaker would have us believe.

This prediction rests upon two theoretical considerations. The first concerns the timing of births. Part of the high birth rate in recent years consists of "business borrowed from the future."

The Census projections, which assume birth rates for each female age group independently of the number of children these women have already had, seem to be very unrealistic. This point has been developed at some length by Pascal Whelpton who estimates that the catching up of postponed births and the advancing of timing of births by younger girls appears to have swelled the number of births during 1946-1955 by between 3,500,000 and 4,500,000. He also presents a method of estimating future births, which does take account of the children which the women in each age group have already had.

What of the future? I don't think I am revealing secrets when I say that the girls who have had three or more children in their 20s are not planning to make any further substantial contributions to the birth rate in their 30s. Thus, for that age group, 30 to 40, the birth rate is almost certain to decline as compared with the past 10 years.

What of the new group in the 20 to 30 age category? The plain fact is that there will be fewer of them because of the exceptionally low birth rate in the 1930's. The number of girls in their middle 20s (the most fertile age group) will not begin to turn up appreciably for about 10 years, and the postwar bumper crop will not make a big impression until about 1971.

My second reason for believing the birth rate will turn down concerns the number of births per family. There has been a trend in recent years towards larger families. I do not think that trend will continue, and I rather expect that there may be some movement in the opposite direction. Most

(Continued on page 40)

The birth rate is likely to turn downward shortly, Mr. Fuchs thinks, we won't increase as rapidly as we have these past ten years and our population won't be quite what many experts have been saying. But the housing boom in the 1970's is sure to come, the crisis in the schools is just beginning—in fact, it will be with us for quite a while as one of the most difficult problems we have to solve. But remember, he cautions, part of the recent high birth rate is "business borrowed from the future."

A Member's Experience With MBA's New Cost Accounting System

And it has been a favorable experience, as his accountant relates here. Since the system was announced nearly a year ago, a number of changes have been made and many of the suggestions which Mr. Dix mentions have been incorporated—such as the servicing department receives a half point on serviced warehoused loans, only net interest figures will be used whether profit or loss, bonuses are included with salaries and profit sharing plan payments are changed to employee benefits. Fifty member firms soon will be recruited to participate in an annual survey, similar to the quarterly Delinquency Survey. Thus, all other members will soon be able to compare their annual costs with the national average which the survey will show.

By **ESPER L. DIX, CPA**
Partner, Livingston, Montgomery & Co., Philadelphia

IN the March, 1956 issue of THE MORTGAGE BANKER, Edward J. DeYoung introduced a standardized cost analysis system for mortgage bankers. The system was developed by the MBA Servicing and Accounting Department, of which Mr. DeYoung is director.

In addition to explaining the many problems that had to be resolved before an acceptable system could be settled on, that presentation showed the data produced by applying the analyses to the operations of 25 mortgage companies of varying sizes. Details of the system were not presented in the article, but all the necessary instructions and work sheets were made available to MBA members upon request.

One of our clients in the mortgage business expressed interest in Mr. DeYoung's presentation, wrote for the instruction material and with our assistance applied it to their operations. As a general rule, we have found that management in most industries is very much interested in comparing operating data with others in their industry, on a non-disclosure basis. The writer feels that the project which Mr. DeYoung's department has launched can be of substantial value to mortgage bankers. It is hoped that this critique will act as an incentive to those who have not yet used the cost analysis and will also help to realize Mr. DeYoung's hope that his presentation would arouse interest in cost data and provide a basis for an improved cost system.

We believe the simplicity of the system is one of its greatest attributes. In fact, it should be made clear to those who have not yet obtained the work sheets, that the analyses are much simpler than one might assume from reading the wealth of data presented in the March 1956 article.

For those who are not familiar with the system, we shall summarize it briefly. A basic premise is established that all income and expense up to the time of delivery of loans to the investor is considered as relating to production, and all income and expense from that time on is considered as servicing. In accordance with this, the company's income is allocated between the production department and the servicing department. With regard to expenses, where there can be a definite allocation between those two departments, this is done. The expenses which cannot be definitely allocated, are summarized into two groups: one to be allocated on an office area basis, and the other allocated on the basis of number of employees. These computations produce the amount of net profit or loss for each of the two departments. Statistics for the production department are obtained as a result of dividing by the number of loans originated during the period, and statistics for the servicing department are obtained as a result of dividing by the average number of loans serviced during the period. The work sheets supplied comprise simply two 8½"x11" sheets. These are easy to follow and are adequately explained in the instructions. To a very great extent, we found the work sheets required only a recopying of data already presented in the company's annual income and expense statement, plus statistics (as to number of loans originated and serviced) which the company already compiled as part of its monthly operating data. The only important information that had to be developed was an allocation of the salary expense. This was done by assigning to production, servicing or administration, the employees listed in the company's payroll record, and then totaling the gross salaries in those three classifications.

Mr. DeYoung stated from the outset that "our recommended cost system is not intended to be used in its exact form for establishing a pure cost accounting system for daily use within an individual company. It is designed, rather, to accumulate cost data which is complete and accurate

enough to provide for the first time, valid and compartive costs throughout the mortgage industry." In our opinion, the system is an excellent development in this direction.

In the March 1956 article, tables were presented giving the data developed by the 25 mortgage companies as a result of applying the cost analyses. These tables showed: (1) the income or loss per loan closed, (2) the net income per loan serviced, (3) the percentages that classes of expense were to total expense, and (4) the percentage allocation of total income and of the total expense, as between the production and servicing departments. The data was given for each individual company and, in addition, averages were computed for the 8 smaller companies, for the 8 medium companies and for the 9 larger companies (classified according to number of loans being serviced) as well as averages for the entire 25 companies combined.

After the data had been compiled for our client in accordance with the system, in comparing our results with those presented for the 25 companies, we diverted in two respects: (1) we refigured their averages on a non-weighted basis, and (2) we refigured their expense classification percentages after excluding interest paid. Our reasoning on these two matters follows.

By referring to Table 1 presented in the March 1956 article, it can be seen that the figure for average profit per loan closed of $10.73 was not obtained by adding up the individual results shown therein for the companies and dividing the result by 25, because such a computation develops an average *loss* of $7 per loan closed. The averages presented in those tables were in effect the average that would be computed if the entire operations of the 25 companies were considered as one. The effect of this assumption can be best illustrated by the following extreme example. Again referring to Table 1 and limiting ourselves to companies numbered 1 and 25, we find:

Company Code Number	Number of Loans Closed Per Month	Net Income or Loss Per Loan Closed
1.	13	$ (34.27)
25.	381	14.44

Computing the average of these two companies, in the manner of the March 1956 article, would result in showing a profit of $12.60 per loan closed. This is a weighted average arrived at by subtracting the products of 331 times $14.44 and 13 times $34.27; then dividing the difference by the 344 total loans. On the other hand, the simple average of these results is a loss of $9.91 per loan ($34.27 less $14.44, divided by 2). In making comparisons of our client with others in the industry, it was our primary desire to compare operating efficiency and we feel that the simple average tells us better how the company's operations compare with the average experience of others. We realize there are arguments for both methods and further discussion on this point is welcome. It may also be of interest to state that we made our comparisons with averages encompassing only two-thirds of the companies, eliminating the one-third most dissimilar in size of operation.

As Mr. DeYoung has already pointed out, interest expense is often a major item to the mortgage banker. His table 3 indicates that, among the 25 companies, interest ranged from being nonexistent to more than double the amount of salaries paid. Therefore, we felt that its inclusion in the total expenses seriously distorted the percentages shown for other classifications of expense. In order to avoid this distortion, we excluded the interest column and computed the percentages of each expense classification to the remaining total. For example, company number 9's interest amounted to 35.6 per cent, and its other expenses to 64.4 per cent (making a total of 100 per cent). To obtain new percentages for the expense items, the percentages given for company number 9 were in each case divided by 64.4 per cent. We were, of course, interested in comparing our client's interest expense, so we did this by finding the percentage of the interest amount to total expenses exclusive of interest. For example, the percentage so computed for company 9 is 55.3 per cent (obtained by dividing 64.4 per cent, total expenses, into 35.6 per cent, interest expense). This gives an indication of the relationship of borrowed money to the size of the operation. If the data had been available, we would have preferred to compare interest expense with the average mortgage inventory.

There was presented in Table 4, percentages of the total income produced by the production department and by the servicing department, and also percentages of total expense allowable to each of these two departments. We fear that these percentages may not be too comparable because they would be greatly affected by whether production brokerages are included as an item of expense (in salaries, for example) or are netted directly against production income. We suggest that the rule be to exclude these brokerages from the expense, and to net them against the production income.

As has been stated previously, it is not claimed that this cost analysis system produces exact departmental costs. However, the only significant point of error we noted could be very simply corrected. This concerns the fact that the servicing department gets no credit for servicing of loans not yet delivered to an investor. This could be corrected by inserting a single line in part II of the work sheet, under the heading of income accounts. On this line there would be made an addition to servicing income and a reduction of production income (without in any way affecting combined income), in an amount computed by applying the going-service-fee-rate to the average mortgage inventory during the period. In our computations we found that such an adjustment resulted in showing an adverse change of 50 per cent in the profit or loss per loan closed, and an increase of 15 per cent in the net income from servicing.

It is our belief that the system as presented, with a few simple refinements, is all that is required by the great majority of mortgage bankers. Any more ambitious undertaking along this line should be a cost system tailored to a single company's operations. We think an attempt to estab-

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Voice of the Correspondent

The Crisis In Our Business

It's a good idea to do some soul-searching from time to time—good for people, for a business, a company, an industry. Forget the accepted notions and start from the beginning to determine if things are exactly as they seem to be. That is what a correspondent has done here, and has come up with the conclusion that the crisis in our business isn't tight money, or the seemingly big problems that face us today; rather it is in some of the practices which, he contends, are being followed by some. What he says will make you stop and think—certainly one cannot be more plain-spoken than he is here.

THE crisis in mortgage banking is not the critical supply of money. The crisis lies in obsolete laws and questionable practices which manifest an apparently spreading lack of integrity which threatens the correspondent system. The challenge to the industry, both lender and correspondent, is to acknowledge unpleasant facts and work in close cooperation to eliminate certain evils which may well destroy the mortgage banking fraternity.

Like most of you, I have found in mortgage banking an opportunity for constructive community service, intellectual stimulation, adequate monetary return and the pleasure of associating with brilliant and dedicated men representing both investors and local correspondents. But despite these rewards, in view of certain malpractices in the business at the present time, I would view with misgiving the entry of one of my sons into the mortgage banking profession.

Let us look at the role of the mortgage banker in the correspondent system. The mortgage banker is entrusted with investing locally the funds of an absentee principal in accordance with general patterns prescribed by that principal. The ultimate investor is active in a great many cities throughout a large geographical area, thus precluding its accurate knowledge of local real estate values and trends in the comprehensive detail required for prudent mortgage lending. Necessarily the investor must rely upon the knowledge and absolute integrity of its correspondent in each locality. As a result, a fiduciary relationship is created, imposing upon the correspondent the strict duty to tell the exact and whole truth in his presentations. While most correspondents sincerely discharge this trust to the best of their ability, there is a definite and disturbing trend — fostered to some extent by obsolete investment laws and thoughtless lenders—for the correspondent to disregard his actual knowledge of local values and in many cases misrepresent the facts in the keenly competitive effort for business in the industry.

Some Cases in Point

Let us look at a few representative —true examples because the facts have been unified.

» Recently we learned from a subdivision developer the reason for his success was that builders in his development could generally obtain from three different mortgage firms \$18,000 conventional loans on houses selling for \$20,000 to \$21,000.

» A broker informed us, in the tight market of December, 1956, that he is having no difficulty in placing 75 per cent conventional loans with several life insurance correspondents.

» A field representative for a large life insurance company advised his local correspondent, during the course of a field trip, that it was satisfactory in connection with conventional residential loans if there was a small second lien as part of the purchaser's equity payment. The correspondent immediately asked for a letter outlining the company's policy to this effect. The field representative replied that he could give no such letter and the second lien should not appear in the loan presentation.

» We all know instances where, because of the exceptionally strong credit of a tenant, investors have made loans and appraisals based solely upon the lease income; consequently, to justify the loan legally, both the correspondent's and investor's appraisers have deliberately "ballooned" physical value far beyond reproduction value. Having joined hands with his investor in this type of intellectual chicanery, it is easy for the local correspondent to rationalize distortions in other aspects of appraising and presentations.

» Many Realtors use dummy purchasers and, unfortunately, sometimes with the knowledge of the local correspondent. One outstanding Realtor in a large city recently advised a local correspondent quite frankly that he needed a full loan, more than legally

permissible, in order to move a certain house; however, the Realtor stated in all seriousness that it would nevertheless be a good loan because the mortgage papers would be signed by a "very strong dummy." If this were not a true case, it would be humorous.

» In an effort to stem these malpractices, investors and correspondents have asked for copies of sales contracts and closing statements from title companies. This has led to the well-known double sales contract and, sad to say, in too many instances misleading closing statements because the title companies cannot be expected to police our industry for us.

The instinctive and defensive reaction to an open airing of these improper practices is to reply that there is a small element of dishonest individuals in any industry or profession. Certainly this is true. However, the medical and legal professions, which are entrusted with our health and rights, have active grievance and ethics committees in local, state and national organizations which are constantly attempting to eradicate the transgressor in their professions. To the contrary, is there a grievance committee in your local or state mortgage bankers association and what action has it taken to improve the moral tone of our industry?

Because of the tremendous building boom which our nation has enjoyed for the past decade, ours has been a mushrooming industry. Obtaining and training the newcomers to our business in the technical aspects of our industry has been a big job. In attending clinics, state and national meetings of the MBA, I have heard very little in the last ten years about the necessity for absolute integrity on the part of local correspondents. Have we too blithely taken for granted this basic principle in view of the great number of new people who have come into the business in recent years?

What has fostered these practices which the overwhelming majority of mortgage bankers decry? It is believed that much of the intellectual dishonesty in the industry is due to obsolete laws which have not kept pace with proven new practices and competitive segments of the mortgage lending business. First, the FHA and, later, the VA introduced wholly new concepts of residential lending not geared to a relatively large down payment or equity on the part of the borrower. Despite the clearly recognized distinction stemming from government guarantees, nevertheless, there is a trend on the part of the lending fraternity as a whole to recognize that the old formula of one-third to 40 per cent equity down payment is not necessarily required in all instances to make a sound residential loan. This has been recognized by laws governing building and loan associations which are permitted to make 80 per cent loans. Life insurance companies and their correspondents are restricted to 60 per cent and 66 2/3 per cent loans by the laws of most states; this competitive disadvantage stimulates duplicity by lenders and local correspondents. Mortgage bankers and their investors should cooperate in each state in a vigorous effort to have the laws changed so that conventional loans may be made legally on a competitive basis with building and loan associations. Once the laws have been changed the need for much of the misrepresentation will be removed.

No sound reason can be given to justify state laws which permit 90 or 100 per cent real estate loans so long as they are made in the guise of debenture financing while the same real estate with the same tenancy is restricted to a 60 or 66 2/3 per cent loan if made as an orthodox real estate mortgage. While the economic approach is the primary criterion of value for income property, many investors look solely to the income flow from nationally rated tenants in underwriting loans. Even though strong credits have been known to fail, we do not quarrel as a matter of policy with any investor taking this approach in underwriting its loans. However, it is believed that the emphasis placed on the economic approach has, in many cases, led lenders and local correspondents to cooperate in exaggerating physical value far beyond reality in order that loans might be made to qualify legally under obsolete laws. The lender who acquiesces in such practices from the correspondent in one case is opening a Pandora box for misrepresentation in all cases. Again the solution of this problem lies in legislation. For example, the State of Iowa permits a life insurance company to make 100 per cent real estate mortgage loans if the credit of the tenant and income stream meet certain prescribed qualifications. The legislature of Iowa has blazed a path which other states may well follow.

The effective way to eradicate these malpractices which stem from intellectual dishonesty, regardless of motivating pressures, is for investors and correspondents frankly to admit that such evils exist and then to work in close cooperation with grievance or ethics committees of local, state and national mortgage bankers associations to clean house. The first giant step is recognition of the problem.

As in the past, the companion columns, Voice of the Home Office and Voice of the Correspondent, are open to anyone with something to say relating to the working relations of investor and originator. It can be a suggestion for improvement, a complaint or the statement of an opinion. Your contribution need not be signed and you are at liberty to take as many words as needed to get across your point of view.

PEOPLE AND PROSPERITY

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observers say that economic circumstances have a large influence upon the number of children that people wish to have. I agree, but it seems to me that the absolute level of income is of little consequence, while the direction and rate of change of income is by far the more important factor. Many people attribute the high birth rate to the prosperity of recent years. It is true that incomes are at record levels. But the really significant point is not that most people are more prosperous than they ever were, but that the rate of increase in income in the past 20 years has been so rapid that they are more prosperous than they ever expected to be. The level of living that people aspire to is determined to a considerable extent while they are quite young. When people say "we can afford to have more children" or "can't afford it," it is usually in terms of material standards which were formed while they themselves were growing up.

The 1930's provide a clear example of this. We are told that the low birth rate of that period can be explained by the fact that people "couldn't afford to have many children." What does that mean? Even in the 30's, the standard of living in the United States was much higher than it has ever been in most of the world. In terms of absolute income, that explanation makes no sense at all. But in relative terms, it does. We know that measured against an aspirational level formed in the 1920's, incomes did seem too low.

What of the Future

What does the future hold in store on this count? It seems highly unlikely that per capita income will increase as rapidly in the next 20 years as it did in the last 20.

We are now at full employment, or close to it. We no longer have a backlog of unemployed as a potential source of increase of output per capita. From now on, the entire increase must come from increased productivity.

If we examine past productivity increases in the various sections of the economy, we find further reason why we should not expect per capita income to grow as rapidly in the next two decades as in the past two. Productivity has risen much faster in agriculture than in either industry or the rest of the economy.

Fewer Farmers

Twenty years ago, one out of every four workers was employed in agriculture. At present, only a bit over 10 per cent of our working population is employed in that sector. Therefore, even if productivity in agriculture should triple in the next 20 years (as it may well do), it can have only a small effect on the over-all total. To some extent this is even true of industry, which employs only about 30 per cent of the labor force. The greatest number of workers, about 60 per cent are not in agriculture or industry, but are in the so-called services sector of the economy. If this country is going to be a great deal richer, healthier, and happier 20 years from now, it will have to be principally because of improvements in this third sector. But this is precisely the sector where productivity gains seem to have been smallest in the past.

I say "seem to have been smallest." because when we talk about productivity in this third sector, there is some question as to whether we know what it is or how to measure it. In agriculture or industry this problem is not as severe. When a worker produces two autos instead of one, or when the same amount of wheat can be produced by half as many men, most reasonable men would agree that there has been an increase in productivity. But what about this all important third sector? Has there been any increase in the productivity of teachers, ministers, doctors or social workers? Do major league baseball players produce more now than they used to? We really don't know the answers to these questions, and what is perhaps more important, we hardly know how to go about getting the answers. As long as we are talking about output in agriculture or industry, we can concentrate on a fairly specific, measurable characteristic—quantity. But when we look at output in the third sector, we have to come to grips with another dimension, quality, and this is something which statisticians and economists find very difficult to measure.

After having gone to some length to show why the rate of population increase may slow down, my reaction to this finding is—So what! Why all this emphasis on counting noses anyway? It would seem to be a great deal more important to be concerned with the quality of our population rather than in the mere quantity.

Promise of the Future

Are we to believe that if the population of this country ever reached a stable plateau, we could no longer look forward to high employment or increasing productivity? It seems to me that there is a misplaced emphasis on the demand side of the question of economic growth, if you are talking about the long pull. I don't think we have come anywhere near satisfying peoples' wants for goods and services. In the short run, demand (that is, effective demand) may fall short, but this is primarily a problem for monetary and fiscal policy. Over the long run, the limiting factor of economic growth is our ability to produce.

COST ACCOUNTING SYSTEM

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lish a much more complicated standard system would discourage its use by many.

We hope the MBA Servicing and Accounting Department can, if it has not already, inaugurate a practice of presenting annual statistics and encourage increasing numbers of bankers to contribute on a nondisclosure basis. This could be done by mailing two copies of the work sheets to members annually; one to be returned without any indication of the company's name. The value of the statistics would be increased if the company is requested to indicate the section of the country in which it is located (6 numbered geographic sections could be established, for example) so that consideration could be given to the varying mortgage markets.

(A copy of Mr. DeYoung's March 1956 article and the cost work sheets, can be obtained by MBA members by writing to the MBA Servicing and Accounting Department, 111 West Washington St., Chicago 2, Ill.)

SECONDARY MARKET

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More than this, I am convinced it must be developed, and maintained, if our free enterprise system itself is to survive. And the question of an appropriate secondary mortgage market is deeply involved in this issue.

How is this issue to be resolved? One thing is certain: if we are to have a secondary market facility within the context of a free market, the first requisite is to create a free market in the world of insured and guaranteed mortgages. By this I mean, basic to anything else, that the interest rates on these mortgages must be as free to move as those of competing types of investments.

The reason for this is simply that, unless the mortgage interest rate is clearly within the range of the market, no secondary facility, though it combined the powers of the Treasury and the Federal Reserve, could meet the demands thrust upon it. When you offer to buy something for more than it is worth, there will be no limit to what is offered you. That is the predicament of FNMA today. Since limits are imposed on rationing by price, FNMA is forced into another form of rationing. It has chosen to limit its purchases to newly made mortgages and, in doing so, abandoned one vital purpose of a true secondary market facility.

Unless the principle of a free interest rate is solidly established the temptation will always exist to try to hold interest rates below the market, on the misconceived theory that this is the only way to achieve desirable social objectives, and then to try to use FNMA, or whatever so-called secondary facility may be devised, to support the misconception. Therefore, a free interest rate is the primary, absolute prerequisite for a true secondary market facility.

The second prerequisite to a secondary market facility is a sound mortgage insurance system. We have the nucleus of that in Section 203 of the National Housing Act as it was originally conceived. The difficulty here is that both within and outside that section, the Act has been so loaded with special insurance operations that are so patently unsound from a market point of view that only by large doses of government support, for which FNMA has had to be the instrument, have they been made to work at all. As MBA has long recognized, these special functions will have to be pared away and FHA restored to the function of insuring marketable mortgages, if the continuous pressure for government support is to be abated.

This question may then be raised: If we have a sound mortgage insurance system and a free movement of interest rates, will there be any need for a secondary facility? Or, to put it another way, is it not possible that a free interest rate is all that is needed to assure a reasonable degree of stability and continuity in flow of funds for soundly insured mortgages? There can be no doubt that the very severe gyrations of insured and guaranteed mortgage activity, as compared with conventional mortgage and other investment activity, have been mainly caused by the interest rate problem. At the same time it may not be justifiable to assume that the elimination of this one problem would result in

the end of all difficulties affecting the flow of mortgage funds.

There is, for example, the problem of over-commitment. The confident planning of housing operations requires that the availability of the funds necessary to finance house sales be firmly determined well in advance. For the institutions called on to make such commitments, however, there are numerous and often unavoidable changes of miscalculation. New savings may not be created as fast as anticipated. Repayments may not be made as rapidly as expected. In either case, institutions may find themselves with more commitments than they can conveniently absorb. A proper secondary facility could help tide over such situations by taking up some of the excess. Such action could not only encourage a more prompt renewal of the flow of new money than might otherwise be the case, but also would lend more confidence and stability to the whole vital commitment process.

There is also the problem of the wide geographic distribution of mortgage funds. Many small savings institutions that would be attracted to remote areas by a satisfactory yield are unable to invest in this manner because of the difficulties they encounter in locating the opportunities and in acquiring mortgages at a distance. A proper secondary facility could well serve the purpose of assembling mortgages for sale to such institutions.

Still another problem is that posed by investors, like pension funds, endowments, and the like, that from time to time may wish to purchase mortgages or obligations secured by mortgages, but that do not wish to be committed to the mortgage market in the same way as are insurance companies or savings banks. Again, a proper secondary facility could provide a means for pooling mortgages for disposition to such irregular investors.

There are still more possible purposes that such a facility might fittingly serve, such as to smooth out purely seasonal variations in the inflow of savings so as to meet the seasonal requirements of construction, to name but one example. The supply of funds for building purposes and for covering the interval between the closing of a loan and the time at which it can be delivered to a permanent investor might also be considered in this context.

All these potential uses of a secondary market facility—to help remedy the problems inherent in over-commitment, to assemble mortgages in remote areas, to pool mortgages for disposition to irregular investors, and to smooth out purely seasonal variations in the inflow of savings—merit the fullest consideration. Others, such as whether or not the facility should provide funds through loans on mortgages as well as through purchases of mortgages, are matters that need to be studied. I should prefer to see these inquiries undertaken by the financial fraternity independently of government. I am sure that among those who participate in the mortgage lending function—the originators, the interim lenders, and the permanent investors—there is enough understanding and ingenuity to settle the issues of the need for, the most suitable form of, and the appropriate functions for, a secondary mortgage market facility.

To make a positive suggestion, I urge that a group, consisting of representatives of MBA, the Life Insurance Association, the American Bankers Association, and the Investment Bankers Association, be created for the purposes of taking on this job. I would also urge that a group so constituted dedicate itself to the proposition that the solution should be found within the resources of our private financial system. In other words, I urge that the private interests involved seek strictly a private answer.

I do not hesitate to put my proposal as I do because I am convinced that there is no other way of reaching a satisfactory answer. Any other point of departure involves the financial participation of government and hence the control of policy by political forces. Experience should have taught us by this time that this simply means the retracing of old steps and taking additional ones down a way that leads inevitably to a government-operated home mortgage credit system.

The signposts are quite clear. Again we have only to look at FNMA. In its present incarnation, FNMA was launched in 1954 to serve a limited function in the private mortgage market under a plan that anticipated ultimate private ownership. Each step taken since that time has carried it away from that function and away from the prospect of private ownership.

If we want private institutions, we must create them privately. If we want a private home mortgage credit system, we shall have to exert ourselves to keep it private. The design of an effective secondary market facility is a good place to begin.

MEETINGS COMING UP

Chicago Conference Will Scrutinize Prospects as Result of Tight Money

Tight money—the principal concern of the mortgage industry the past year and now a worrisome consideration for other areas of industry—can't help but be the principal item on the agenda at the Association's forthcoming Midwestern Mortgage Conference, Conrad Hilton Hotel, Chicago, February 19-21.

This Conference, the first of a series of three in the first half of 1957, is usually our largest regional meeting. Attendance this year is estimated at around 1500—but it could run higher in view of the more than ordinary interest in what is ahead in the field of money and credit. MBA winter meetings are usually considered opportunities to gauge the future and appraise the prospects for the coming twelve months, and this is probably more true in 1957 than ever before.

The Conference this year is something a good deal more than a discussion of the mortgage business—rather it is a group of meetings, led off by a Farm Mortgage Clinic and luncheon, Tuesday, February 19, followed by a day and a half of Conference, with the final afternoon given over to a discussion of the mortgage business sponsored by the Young Men's Activities Committee and then concluding with the regular winter board of governors meeting.

The Farm Loan Committee, headed by Roy C. Johnson, chairman, and president of the Albright Title & Trust Company, Newkirk, Oklahoma, has organized an unusually timely farm mortgage program to begin with a luncheon. The principal speaker will be Thomas A. Maxwell Jr., Director, Land Bank Service, Farm Credit Administration, Washington, D. C., on "Today's Operations of the Federal Land Bank System".

Following this, a group of authorities from various areas of the farm loan field will get together for a panel discussion and a look at conditions in the farm loan field. They include:

James H. Albright, manager, Albright Investment Company, Winfield, Kansas.

Douglas K. Schnell, vice president, Fargo Investment Company, Fargo, North Dakota.


G. W. Mitchell


J. S. Baughman


Bentley McCloud


Walter Nelson


Roy C. Johnson


W. A. Clarke


Lon Worth Crow


B. B. Bass

Eliot O. Waples, vice president, Midland Mortgage Company, Cedar Rapids, Iowa.

Carl M. Adams, superintendent, farm loans, Equitable Life Insurance Company of Iowa, Des Moines.

Lester B. Foreman, manager of farm loan department, Business Men's Assurance Company, Kansas City, Missouri.

Paul A. Meyers, treasurer, Lutheran Mutual Life Insurance Company, Waverly, Iowa.

The Conference program opens at 10 Wednesday morning, with Bentley G. McCloud, Jr., vice president, The First National Bank of Chicago, presiding. Walter C. Nelson, chairman of the MBA Clinic committee and president, Eberhardt Company, Minneapolis, will make the opening talk.

Speakers include President John F. Austin, Jr., speaking on "Prospective Developments in the Mortgage Market", and James R. Price, president, National Homes Corporation, Lafayette, Indiana, speaking on "The Prefab's Role in Home Building Today".

At the second session that afternoon, the discussions will turn to internal mortgage matters. The specific theme is "Developing New Sources of Income for the Mortgage Banker".

M. J. Mittenthal, president, N. E. Mittenthal & Son, Inc., Dallas, will speak on "Insurance Can be Profitable". B. B. Bass, president, American Mortgage and Investment Company, Oklahoma City, will speak on "What Streamlined Servicing Means Profit-Wise".

The final feature of the afternoon will be a panel discussion on "Making the Most of Your Most Valuable Business Asset — Your Personnel." John C. Hall, MBA vice president, will be moderator. Participants will be:

Lon Worth Crow, Jr., president, Lon Worth Crow Company, Miami.

W. A. Clarke, president, W. A. Clarke Mortgage Co., Philadelphia.

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Francis C. Little Heads Capital MBA

Francis C. Little, senior vice president of B. F. Saul Co., was elected president of the Metropolitan Washington, D. C., MBA.

Other officers selected were:

Vice president, A. Britton Browne, Jr., executive vice president of Randall H. Hagner & Co.; secretary Robert McIntosh, partner of McIntosh & McIntosh; treasurer, Roger W. Hatch, vice president of Walker & Dunlop, Inc., and general counsel, H. Loy Anderson.

Elected to one-year terms on the board of governors were William F. Bergmann, vice president, Arlington Realty Co., and Fredrick X. Wilson, assistant vice president, Suburban Trust Co.

Chosen for two-year terms were John Holzberg, vice president, Shannon & Luchs, and James A. Graham, senior vice president, Frederick W. Berens Co.

The officers and elected members form the board of governors. These past presidents are also honorary members of the board: Martin R. West, Jr., vice president, Weaver Bros. Inc., the retiring president; William E. Shannon, president, Shannon & Luchs, and George W. DeFranceaux, president of Frederick W. Berens Co.

President West submitted to the Association an account of the past year, which he described as very active. He told of meetings with the FHA and VA and the holding of clinics with the National Housing Center. In addition, he said, numerous talks to business groups were given about the activities of the Association.

The Association's membership has grown to 200 persons, representing 43 organizations. They represent the principal mortgage banking companies, the larger commercial banks and local life insurance companies.

Although one of the younger local associations, the Washington MBA's present membership put it right at the top among the larger groups.

The third and final session of the Conference proper will feature four addresses:

Charles E. Sigety, FHA deputy commissioner, Washington, D. C., speaking on "FHA's Plans and Projects".

J. Stanley Baughman, president, Federal National Mortgage Association, Washington, D. C., speaking on "FNMA's Role in Today's Mortgage Market".

Honorable Ed Edmondson, Representative, 2nd District, State of Oklahoma.

George W. Mitchell, vice president, Federal Reserve Bank of Chicago, speaking on "Savings and the Capital Markets in 1957".

The last afternoon has been staked out by YMAC—and those members who have attended some of the previous meetings organized and executed by the young men's group know that a lively and spirited session is in prospect. As is natural for young men with youthful enthusiasms, they plan to go down to bedrock in exploring some of the current mortgage problems. It is something that every member who attends the Conference will not want to miss.

Members have received the Association's tentative program with hotel and advance registration cards as well as a ticket reservation form for the Farm Mortgage Clinic. All should be processed immediately. As seems to be usual these days regardless of where we are meeting or what time of the year, hotel accommodations are never plentiful. This means that to get what you want you should not delay in making your plans. The registration fee is $15 which covers the entire three days except for the Farm Mortgage Luncheon.

Jerry B. Frey, Jr. Named Head of Dallas MBA

Jerry B. Frey, Jr., partner in the Brown-Frey Mortgage Company, Dallas, was elected president of the Dallas MBA for 1957 succeeding Aubrey M. Costa, president, Southern Trust and Mortgage Company. Other officers elected were Carl S. Davis, vice president, J. E. Foster & Son, Inc., as vice president; and John E. Driscoll, Jr., Guillot Mortgage Company, as secretary-treasurer. In the photo above, President Frey (second from right) is congratulated by Mr. Costa with Mr. Davis (left) and Mr. Driscoll (right).

Mr. Frey has served on numerous MBA and Texas MBA committees. In 1955, he was awarded the MBA Certificate of Merit; and in 1956, he served as the first chairman of the Southwestern Senior Executives Conference, held in cooperation with SMU. Currently, Mr. Frey is chairman of the educational and public relations committees of the Texas MBA; and, also, is serving on the national MBA educational, public relations and Southwestern Senior Executives Conference committees.

Chicago MBA Begins 41st Year

Oldest local MBA begins fourth decade of service to the industry of its area

It was an occasion to record—a local mortgage association passes its 40th birthday, making it just a few years younger than MBA. The occasion was the 1957 annual dinner meeting of the Chicago MBA, oldest local mortgage group in the country. For periods during its history it has also been the largest but, as of today, Texas MBA has more members.

Chicago MBA was formed in December, 1916 and was known as the Chicago Mortgage Bankers Club. It was incorporated in 1920 under its present name.

Two of the original members, William J. Hoppe, who has his own mortgage firm, and Byron V. Kanaley, of McElvain Mortgage Company, are still active in the association. Kanaley was president of the group from 1916 until 1920 and formerly was MBA president.

Texas MBA's beginning closely parallels that of the Chicago MBA. It was organized in February 3, 1917 in Dallas as the Texas Land Mortgage Bankers Association and in 1930 became the Texas MBA. MBA itself was originally organized as a farm mortgage bankers association.

At Chicago MBA's anniversary, Gov. William G. Stratton of Illinois, Chicago Mayor Richard J. Daley, MBA Secretary George H. Patterson, Thomas Coulter of the Chicago Association of Commerce, John H. Down of the Chicago Metropolitan Home Builders Association, Myron H. Fox

Chicago MBA's officers with, left to right, MBA President John F. Austin, Jr.; Robert H. Pease, new vice president; John Womer, retiring president; Helen M. Lawler, executive secretary; Hoyt Thompson, president; and Stephen Cohn, secretary-treasurer. Interviewer: Earl Weber, *Chicago American*. Right, above, Irvin R. Schildein; Paul Goodrich; MBA Secretary George H. Patterson; and Harold Moore having their picture taken by Phil Gundermann of *Real Estate News*.

Below, standing, Howard Green, Maurice A. Pollak, Delmar Beaumont, Harry Fisher and Harold Yegge with, seated, Leroy Pape and Joseph Grayson being interviewed by Charles Heath of *Construction News*.

Another interview: Robert Seise, president, Illinois MBA; John F. Austin, Jr., president, MBA; John Womer, retiring Chicago MBA president; and Hoyt Thompson, new Chicago MBA president with Al Jedlicka, Jr., *Chicago Daily News*, conducting the interview.

of the Cook County Council of Insured Savings Associations and Frank Lynn of the Chicago Real Estate Board all congratulated the organization for its accomplishments and service to the mortgage industry.

MBA President John F. Austin, Jr., was the principal speaker at the Chicago group's dinner.

If announced plans for the expansion of the nation's capital plant, both private and government, are realized, then we can expect the present "tight money" situation to continue for the remainder of this decade and perhaps longer, President Austin said. He added that the most severe strain resulting from tight money has been in the field of residential mortgages.

"This means a rough kind of adjustment for those of us who are seekers of mortgage funds. We may as well admit it, we've been spoiled by easy money. We've had it with only brief interruptions since the 1930's. Until fairly recently the trend in interest rates has been down and every proposal for easing credit has met with ready takers.

"But now things are different and I think for some time to come they are going to keep on being different. The terms of the bargain are going to be set on the other side of the table. Lenders are, and will continue to be, more selective. They are being selective because they have no other choice. All comers can no longer be satisfied. There are simply too many of them. Lenders have to raise standards as well as rates in order to ration even a growing volume of available funds amid the greatest upsurge of peacetime capital demands that has ever occurred in the history of this country."

We will have to live with conditions as they are now and as they are likely to be for some time, he said.

"Our problem, therefore, is that of learning to live with tight money rather than hoping vainly to find some escape from it. Until the economy itself begins to pause for breath, and until some unused capacity is evident and some slack exists in material resources, relaxations of credit by either direct or indirect methods offer a very delusive sort of machine.

"The coming year should be a good one for conventional lending. This seems especially true of loans on commercial and industrial properties. It should also be true in the area of conventional residential loans, where activity has been notably stable. It may reasonably be expected that a greater volume of conventional home mortgage funds will be available this year than last. The big question concerns the FHA and VA loan markets; FHA's action of last December raising the rate allowed on loans insured under Section 203 has not, as yet, produced a strong market for these loans. The future of the VA loan can only be described as uncertain."

Hoyt Thompson President

H. Hoyt Thompson, Ward Farnsworth and Co., was elected president of Chicago MBA succeeding John R. Womer. Robert H. Pease, Draper and Kramer, Inc., was elected vice president. Stephen G. Cohn, Greenebaum Mortgage Company, was elected secretary-treasurer.

Members of the board elected for terms ending 1959 included Laurence H. Cleland, Baird & Warner, Inc.; William E. Findeisen, Pacific Mutual Life Insurance Co.; James D. Green, The Northern Trust Company; Donald J. Griffin, Chicago Title and Trust Company; Robert J. Newman, Coonley and Green, Inc.; Marvin A. Reynolds, Merchants National Bank in Chicago; and Robert H. Wilson, Percy Wilson Mortgage & Finance Corporation.

Morris Levinkind, Kahn-Levinkind, Inc., was elected to fill a vacancy ending in 1958.

There are more local mortgage associations in the country now than there has ever been in the past, a total of forty-four scattered over the country. Of these, 17 are state or sectional groups, including the MBAs of Arizona, Arkansas, California, Northern California, Southern California, Florida, Central Florida, Illinois, Iowa, Louisiana, New Jersey, North Carolina, Oklahoma, Texas, Utah, and Wisconsin. The remainder are local associations, including those in Atlanta, Baltimore, Birmingham, Charlotte, Chicago, Cleveland, Dallas, Denver, Detroit, Greater Miami, New York City, Palm Beach County, Florida, Fort Worth, Houston, Indianapolis, Kanawha County, West Virginia, Kansas City, Lubbock, Memphis, Minneapolis, Milwaukee, Philadelphia, Pittsburgh, St. Louis, St. Paul, Seattle, Washington, D. C., and Columbus.

With a few exceptions, all of the local associations are active and hold regular meetings throughout the year with the exception of the summer months. The state associations are particularly active, concerning themselves with matters pertaining to their own areas and do a creditable job of studying state legislation. It is the state organizations which are likely to take the lead in pressing for needed reforms in the mortgage industry, such as modernization of foreclosure and mortgage laws.

OPPORTUNITY FOR BANKS

(Continued from page 20)

and demand, they follow the money market, and they're not tied to any artificial restrictions dictated by politics. These mortgages are strictly on a par basis and, consequently, no phoney discounts are involved.

The cost of acquisition is less. Your year-to-year income is more stable and more continuous. And you don't have all the red tape and the constant handling that take up so much time and costs so much money as is true for insured and guaranteed loans. The borrower has more equity in his home, he's a better credit risk and better pay, so servicing is less expensive and there's less chance for foreclosure. No wonder the banker is willing to assume his own risk.

Without the shackles of FHA and VA the banker can do a better job for his borrowers. And since your borrower doesn't have a paternalistic government breathing down his neck, he feels a lot closer to his banker and is much more inclined to ask about other financial matters.

As it now stands, the new look conventional loan is meeting today's stringent mortgage requirements without a hitch.

As bankers, we've got a unique opportunity to befriend the home purchaser, to help the builder, to build up our own banks and, at the same time, to develop our community and strengthen the national economy.

What can we do to make the most of it?

» We can provide the home pur-

Robert E. Smith Is New Jersey MBA Head

Newly-elected president of the New Jersey MBA is Robert E. Smith, second vice president of the Mutual Benefit Life Insurance Company, Newark. Prior to his appointment as second vice president, he had been city mortgage manager.


Robert E. Smith

He is vice chairman of MBA's educational committee and a member of the conventional loan committee and the clinic committee.

One of his major enthusiasms is the widening of a sound educational base in the mortgage banking field. He serves as an instructor in a mortgage banking course being offered jointly by the Rutgers University Extension Division and the New Jersey MBA.


A milestone in the educational program of the New Jersey MBA—the first class to be graduated from the course in mortgage banking sponsored by the Association and Rutgers. Seated, center, is Philip Zinman, outgoing president, holding the diplomas to be awarded. I. Hamilton Stillwell, of Rutgers, holds the diplomas along with Zinman. To Zinman's right is Samuel Farb, vice chairman of the educational committee.

Other officers elected were: First Vice President, Frederick C. Stobaeus, Vice President, National Mortgage Co., Newark; Second Vice President, Raymond A. Mulhern, Vice President, Underwood Mortgage and Title Co., Irvington; Treasurer, Charles A. Horn, Vice President, National State Bank of Newark.

Diplomas were awarded at the meeting to students who had attended the course in mortgage banking spon-

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chaser with a mortgage which fits his needs and his pocketbook or we can help him get it from some one else. A construction loan will make his life much easier; and some sound financial advice, at the right time, can save many a heartache.

» We can get to know the builder better. We should help him to understand that the price of money should fluctuate with changes in supply and demand. We can paint the picture so he'll realize that bigger down-payments and shorter terms mean more dollars for more house-starts and that he's really on the receiving end of the bargain. That's the kind of talk he understands, but we've got to prove to him in black and white that we're not trying to sell him a bill of goods.

» We can shift into high in our own mortgage operation. Mortgage lending just can't help but build business for the bank. A strong, aggressive mortgage department will bring in new customers, will make friends in the community, will sell other bank services, and will add materially to the profit account.

The big opportunity is here today. Strike while the iron is hot.

YMAC

Column sponsored by the Association's Young Men's Activities Committee
Cary Whitehead, Memphis, Vice Chairman
Joe Jack Merriman, Kansas City, Mo., Vice Chairman

Again this year, MBA's Young Men's Activities Committee will offer in a number of issues of *The Mortgage Banker* items of interest to the younger men of the mortgage business. The space will be used for a twofold purpose: first, to keep everyone abreast of events, developments, and planned programs of YMAC; and, second, to present articles of general interest. Several of these are now in preparation for future issues including such topics as a young man's future in a life insurance company mortgage loan department and the future of a young man in the commercial mortgage field. Look for these in coming issues.

One of the most valuable opportunities available to the young men in the mortgage banking industry is the excellent series of regional meetings which MBA provides each year. MBA's annual Conventions have grown into large affairs, so large in fact that it is no longer possible for the average person to cover all the ground he would like to. The MBA regional Conferences and Clinics, however, are a bit different and offer excellent opportunities for our group to get to know others in the industry.

In line with the various conferences and clinics sponsored by MBA, YMAC is conducting a series of programs at each of the meetings designed especially for the young men. Be sure to attend and share your thoughts with the others. In addition, a sub-committee has been designated to work with the MBA Trust Committee in visiting the various colleges and universities throughout the country so as to interest the young college graduates in entering the mortgage field. A panel discussion of current mortgage problems is being sponsored by YMAC in connection with the Midwestern Mortgage Conference in Chicago, so be sure to make your plans to attend this session.

E. C. Greene

John W. Weber, vice president, real estate and mortgage loan investment, Bankers National Life Insurance Company, Montclair, New Jersey, retired as of December 31. Mr. Weber jointed Bankers National Life in 1927 as supervisor of the Dollar Monthly plan, which was at that time a new departure in life insurance protection. Before being made vice president in 1955, he served as assistant treasurer and second vice president for the Company. Previously he was with New York Life and Berkshire Life.

Carl A. Robinson and Company, Memphis, has been consolidated with **Percy Galbreath and Son, Inc.,** of the same city. Mr. Robinson has been elected chairman of the board. W. D. Galbreath is president and J. J. Heflin, Jr., is vice president.

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sored by the Association and the Extension Center of Rutgers University in Newark. The students who completed the course were specially-selected employees of member institutions of the MBA throughout the state.

In commenting on the completion of this first course, Philip Zinman, outgoing president, declared:

"This marks a tremendous achievement in the history of the association—an accomplishment even more significant than we realize. Through the dedicated work of several of our members, a curriculum has been established providing a sound educational base for mortgage banking principles."

Zinman singled out Norman P. McGrory, Vice President of the Howard Savings Institution, Newark, Chairman of the MBA's Educational Committee, and Samuel Farb, Treasurer of the National Mortgage Co., Vice Chairman, for commendation in putting the course into operation. He also praised the efforts of I. Hamilton Stillwell, Director of the Newark Extension Center of Rutgers University in making the university's services available for this educational program.

Walter C. Kautz, Cincinnati, has been promoted to mortgage loan secretary for the Ohio National Life Insurance Company. Mr. Kautz, an officer aboard the U.S.S. Pensacola during World War II, attended Denison University and the University of Cincinnati Evening College where he graduated with honors in 1952. He is a member of the Junior Chamber of Commerce, Society of Residential Appraisers, an Associate of the Life Office Management Association and active in MBA's Young Men's Activities Committee. He joined the Ohio National Life in 1946 and has served as mortgage loan supervisor since 1952.


Walter Kautz

Miles C. Babcock has been appointed vice president and mortgage officer of Teachers Insurance and Annuity Association of America and its companion organization, College Retirement Equities Fund, R. McAllister Lloyd, president, announced. **Wilfred J. Wilson** was named associate secretary.


Miles C. Babcock

Prior to joining TIAA-CREF in 1954, Mr. Babcock was associated with Prudential for seven years. During World War II, he served in the U. S. Navy and was commissioned lieutenant (j.g.). He took his B.A. degree at the University of Washington.

Mr. Wilson joined TIAA-CREF as assistant secretary in 1956. Previously, he had been an officer in the law department of the Great-West Assurance Company of Winnipeg. He served with the Royal Canadian Artillery during World War II and took his B.A. at the University of Toronto.

Formation is announced of the firm of **Eleford & Rutgers, Inc.,** New York, principals of which are Jack Eleford and Ernest Rutgers, both formerly with Pringle-Hurd & Co. Eleford & Rutgers will represent Sonoma Mortgage Corporation in New York.

Trustees of West Side Savings Bank, New York, announced the advancement of **George E. Transom, Jr.,** from assistant mortgage officer to mortgage officer. Mr. Transom is active in mortgage circles, currently serving as Secretary to the New York Chapter, Society of Residential Appraisers and Savings Bank Real Estate and Mortgage Forum of Groups IV and V. Elected to assistant secretary was **Peter A. Clemente**, formerly assistant manager and now Manager of a West Side Savings Bank branch office.